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FORM 10-K

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1997
OR

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

COMMISSION FILE NUMBER 0-19871

CYTOTHERAPEUTICS, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE	94-3078125
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

701 GEORGE WASHINGTON HIGHWAY, LINCOLN, RI 02865
(Address of principal executive offices) (zip code)

Registrant's telephone number, including area code: (401) 288-1000

Securities registered pursuant to Section 12(b) of the Act:
NONE

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

COMMON STOCK, $.01 PAR VALUE

Title of class

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or l5(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes /x/ No / /

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

Aggregate market value of Common Stock held by non-affiliates at March 9, 1998: $49,641,229. Inclusion of shares held beneficially by any person should not be construed to indicate that such person possesses the power, direct or indirect, to direct or cause the direction of management policies of the registrant, or that such person is controlled by or under common control with the Registrant. Common stock outstanding at March 9, 1998: 18,264,522 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement for its 1998 Annual Meeting of Shareholders are incorporated by reference into Part III of this Report.

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FORWARD LOOKING STATEMENTS

This report contains certain forward-looking statements regarding, among other things, the Company's expected results of operations, the progress of the Company's collaborations, product development and clinical programs, the need for, and timing of, additional capital and capital expenditures, collaboration prospects, costs of manufacture of products, the protection of and the need for additional intellectual property rights, regulatory matters, the need for additional facilities and potential market opportunities. The Company's actual results may vary materially from those contained in such forward-looking statements because of risks to which the Company is subject such as risks of delays in research, adverse results from the Company's development or clinical testing programs, obsolescence of the Company's technology, lack of available funding, competition from third parties, termination of the Company's collaborations, intellectual property rights of third parties, unavailability of needed raw materials, failure of the Company's or its collaborators to perform, litigation, regulatory restrictions, and other risks to which the Company is subject; see "Cautionary Factors Relevant to Forward-Looking Information" filed herewith as Exhibit 99 and incorporated herein by reference.

ITEM 1.

BUSINESS

THE COMPANY

CytoTherapeutics, Inc. ("CytoTherapeutics" or the "Company") is a leader in the development of novel cell therapies designed to treat human diseases. The Company is developing products based on two principal technologies: encapsulated-cell therapies and stem cell therapies. The Company's encapsulated-cell therapies are based upon the use of living cells encapsulated in the Company's membranes and inserted into specific sites in the body; the Company's stem cell therapies are based on the use of unencapsulated human stem cells to replace or repair damaged or defective cells. The Company is currently developing encapsulated-cell products for the treatment of chronic pain and Parkinson's disease with additional research efforts directed to other disorders. The Company has initiated a research and development program for neural stem/progenitor cells and has also established a research program to discover the stem cell of the pancreas and the liver. In addition, the Company has encapsulated-cell research programs ongoing with respect to ophthalmic diseases. The Company currently has one product candidate in clinical trials: its encapsulated-cell implant to treat chronic pain.

CytoTherapeutics, Inc. was incorporated in Delaware in 1988 and currently has one subsidiary, StemCells, Inc., a California corporation acquired by the Company in September 1997.

THE UNMET NEED

Biotechnology has discovered or created a number of new and promising proteins, but the lack of an effective way to deliver these proteins locally has limited their widespread use. The Company believes its encapsulated-cell therapies may provide a platform for effective local delivery of these and other proteins to treat diseases. Many diseases result from organ failure where organs cannot be transplanted to cure the disease (e.g., neurodegenerative diseases and pancreatic failure) or where there are constraints due to a short supply of organs for transplant. The Company believes its stem cell technology may provide the basis for replacing certain lost or damaged cells. If the Company can successfully develop either or both of its cell therapy technologies, it believes that its technologies may provide the basis for addressing a number of diseases with significant unmet medical needs.

CELL THERAPY BACKGROUND

ROLE OF CELLS IN HUMAN HEALTH AND TRADITIONAL THERAPIES

In healthy individuals, cells maintain normal physiological function by secreting or metabolizing substances, such as sugars, amino acids, neurotransmitters and hormones, which are essential to life. When cells are damaged or destroyed, they no longer produce, metabolize or accurately regulate critical molecular substances required by the body. For example, the progressive decline common to many neurodegenerative diseases, such as Parkinson's disease and amyotrophic lateral sclerosis ("ALS"), is associated with impaired cellular function.

Recent advances in biotechnology have led to the discovery of a number of specific proteins that are, in certain diseases or disorders, inadequately produced by the body's own cells. While these proteins overcome some of the limitations of traditional pharmaceuticals, such as lack of specificity, they do not reproduce the natural ability of cells to secrete such substances at the precise sites of action and in the appropriate physiological quantities or for the duration required. As a result, investigators have considered using cell therapy to replace vital cells which are failing by implanting cells which carry the ability to provide a needed critical molecule or by implanting cells to replace those which have failed. In situations of

irreversible failure of vital cells, transplantation of cells offers the possibility of replacing the functions of these failed cells, thus potentially restoring health.

THE POTENTIAL OF CELL-BASED THERAPY

Cell-based therapy, the use of cells to treat diseases, has the potential to provide a broad therapeutic approach of comparable importance to traditional pharmaceuticals and the more recently developed genetically engineered biologics. However, autologous cells (cells from the individual into whom they are to be transplanted) are available in limited supply, may be abnormal if the patient is ill and often can only be obtained through significant surgical procedures. Allogeneic (same species) cellular transplants and xenogeneic (cross-species) cellular transplants generally require the use of potent immunosuppressive drugs. These drugs broadly compromise the patient's immune system in order to decrease the likelihood of rejection of the transplanted cells and expose the transplant recipient to adverse side-effect(s), such as increased risk of infection or cancer. CytoTherapeutics believes its encapsulation technologies may reduce or eliminate the need for immunosuppression, as well as allow site-specific delivery and relative control of cell output. CytoTherapeutics believes its unencapsulated stem cell technologies may provide a way to replace specific cells that have been damaged or destroyed. This approach may be necessary when cell replacement requires repair of cellular architecture or direct cell-to-cell contact. Such replacement with stem cells, which may grow and differentiate to produce differentiated progeny (i.e., mature, lineage-restricted cells), may allow for the restoration of function through the replacement of normal cells where this has not been possible in the past.

CYTOTHERAPEUTICS' PORTFOLIO TECHNOLOGIES: ENCAPSULATED-CELL THERAPIES AND STEM CELL THERAPIES

ENCAPSULATED-CELL THERAPIES

Encapsulated-cell therapies represent a potentially broadly applicable delivery platform for treating a number of diseases which are currently untreatable or poorly treated with present technologies. The Company is employing its proprietary encapsulation techniques to develop semipermeable polymer implants containing living cells which are designed to be placed into selected sites in the body to treat specific diseases or conditions. The implants are also designed to allow nutrients to reach the encapsulated cells and to allow wastes and the therapeutic protein(s) to pass out of the implant while protecting the cells from elements of the patient's immune system.

The Company's implants are designed to be biocompatible, remaining in contact with the recipient's tissues without generating a response that would significantly inhibit the functioning of the encapsulated cells or cause significant injury to host tissues. When such biocompatibility is achieved, the membrane can selectively permit nutrients and oxygen to pass from the recipient through the membrane into the implant, nourishing the cells and allowing them to function. Similarly, such biocompatibility, together with the permeability of the membrane, enables the substances produced by the encapsulated cells to pass through the membrane and produce the desired therapeutic effect.

ADVANTAGES OF THE COMPANY'S ENCAPSULATED-CELL THERAPIES

Many diseases have no satisfactory treatment today, in certain cases, because therapeutic substances generally do not reach the required sites in appropriate concentrations when administered by conventional methods. The Company believes that its encapsulated-cell technology represents an approach that may offer a number of advantages over other forms of delivery for therapeutics.

SITE SPECIFIC DELIVERY

Researchers have identified a number of substances which may be beneficial in the treatment of human disorders. However, it has been difficult or impossible to find a safe and effective way to deliver

many of these potent substances to the required sites at the required concentrations and at reasonable costs. Systemic delivery, such as oral or intravenous delivery, may cause significant side-effects since very potent molecules are being delivered to sites in the body where they are not normally present or needed. This is especially likely where large amounts are administered systemically to achieve therapeutic levels in the central nervous system ("CNS"). A recent clinical trial of a new protein, CNTF, sponsored by another company, for example, resulted in significant side-effects after systemic administration.

In contrast, CytoTherapeutics' cell-containing devices are designed to deliver these therapeutic substances to specific locations where they are needed, thus avoiding many of the side-effects associated with conventional routes of administration. This form of delivery should result in better therapeutic ratios--reflecting an ability to provide effective doses with lower toxicity. In addition, because the therapeutic substances are produced by living cells sustained within the implant, these substances potentially may be delivered over extended periods of time. The production of these substances at the site of action eliminates the problems of drug stability which hampers effective treatment with pumps and polymer carriers.

RETRIEVABILITY

The Company's implants are designed with a tether at the end of the active portion of the implant to allow them to be retrieved with relative ease. By exposing the tether, which is sutured below the skin, and withdrawing the device, a physician should be able to retrieve or replace the implant. Should complications arise, or if a new implant is desired, a physician should be able to retrieve the capsule. Moreover, the capsule keeps the cells in the location intended as opposed to unencapsulated cells which cannot be so constrained.

DELIVERY OF MULTIPLE SUBSTANCES

The Company's implants may also provide the advantage of delivering multiple therapeutic substances simultaneously at a single site. The Company believes that such an ability could lead to development of improved therapies. The Company's implant to treat chronic pain is one such example of delivery of multiple substances.

GENE THERAPY

The Company believes that its encapsulated-cell therapies may provide an effective way to deliver gene therapy: the use of encapsulated cells to deliver genetic information over an extended period may be able to increase the efficiency of gene transfer to the host and hence improve the effectiveness of gene therapy. In addition, the implant could be retrieved, if desired or required. The Company does not presently have commercial access to any such genes for use in gene therapy.

There can be no assurance that the Company will successfully develop its encapsulated-cell therapies commercially or that, if successfully developed, it will achieve the benefits described above or that the advantages of such technology will be greater than the potential disadvantages.

STEM CELL TECHNOLOGY

Stem cells may be functionally characterized as cells whose progeny include, both daughter stem cells (by self-renewal) as well as more differentiated cells. Stem cells exist in humans as a self-renewing source of cells needed in the various systems of the body (e.g., hematopoietic, neural and neural crest, hepatic, pancreatic endocrine cells, and mesenchymal stem cells). These rare, self-renewing stem cells are present in many tissues and are responsible for organ regeneration after injury or during normal cell replacement. The Company believes that these cells can form the basis of therapies which have the potential to replace specific subsets of cells that have been injured or lost through disease, injury or genetic defect.

The Company is seeking to identify, isolate and find methods of expanding a variety of different human stem cell cultures for use in treatment of a variety of human disorders. The Company believes that there are a finite number of stem cells in the human system and that it is possible for the person or entity that first identifies and isolates a given stem cell culture to obtain patent protection for such cells. The Company's strategy is to be the first to identify, isolate and patent multiple types of human stem/progenitor cell cultures with commercial importance.

Neurodegenerative diseases such as Parkinson's disease, ALS and Alzheimer's disease affect a significant portion of the U.S. population and currently have no effective long-term therapies. The Company believes that its neural stem/progenitor cells may be useful in treating such diseases. The Company is continuing research into, and has initiated the development of, its human neural stem/ progenitor cell-based therapies.

The Company has also initiated research programs to discover the human pancreatic islet stem cell and the liver stem cell. Pancreatic islet stem cells may be useful in the treatment of Type 1 diabetes. Liver stem cells may be useful in the treatment of diseases such as hepatitis, cirrhosis of the liver and liver cancer.

There can be no assurance that the Company will successfully develop its stem cell therapies commercially or that, if successfully developed, it will achieve the benefits described above or will achieve benefits therapeutically equal to or better than the standard of treatment at time of testing or that the advantages of such technology will be greater than the potential disadvantages.

ADVANTAGES OF THE COMPANY'S STEM CELL TECHNOLOGY

NO OTHER TREATMENT

To the best of the knowledge of the Company, no one has developed an approved method for replacing lost or damaged tissues from the human nervous system; replacement of tissues in other areas of the human body is limited to those few areas where autologous transplantation is now feasible; in a few additional areas, allogeneic transplantation is now used, but is limited by the paucity of organs available through donation. The Company believes that its stem cell technologies have the potential to reestablish function in at least some of the patients who have suffered the losses referred to above.

NATURE OF REPLACEMENT CELLS

The Company believes that stem cells can self-renew and differentiate into the multiple kinds of cells that are commonly lost in, for example, neurodegenerative diseases. Transplantation of these stem cells may allow these cells to migrate limited distances to the proper location within the body, to expand and differentiate and to replace damaged or defective cells. If the Company can show that the foregoing process occurs, the cells that are substituted could form new cells that could facilitate the return to proper function. The Company believes that such replacement of damaged or defective cells by functional cells is unlikely to be achieved with any other treatment.

PRODUCT DEVELOPMENT PROGRAMS AND RESEARCH EFFORTS

OVERVIEW OF RESEARCH AND PRODUCT DEVELOPMENT STRATEGY

The Company believes that its encapsulated-cell technology can be used to deliver a wide variety of therapeutic substances or vital cells to the sites where they are required. The Company's lead product, its implant for treatment of chronic pain, is designed to provide a new means of delivering substances with known therapeutic effects directly to the CNS. The next group of proposed products in the Company's pipeline seeks to build on the Company's expertise in encapsulating living cells that deliver therapeutics directly to the CNS for the treatment of such chronic and disabling CNS disorders such as Parkinson's

disease. The Company has also established a program to look at potential treatments for diseases of the eye, based on its encapsulated-cell technology. In addition, the Company is attempting to isolate and develop a series of stem/progenitor cells to serve as a basis for replacing diseased or injured cells, especially cells of the human nervous system, liver and pancreas.

The following table lists the potential therapeutic indications for and current status of CytoTherapeutics' primary product development programs and research projects and is qualified in its entirety by reference to the more detailed descriptions of such programs and projects appearing elsewhere in this Report. The Company continually evaluates its research and product development efforts and reallocates resources among existing programs or to new programs in light of experimental results, commercial potential, availability of third-party funding, likelihood of near-term efficacy, collaboration success or significant technology enhancement, as well as other factors. The Company's research and product development programs are at relatively early stages of development and will require substantial resources to commercialize. There can be no assurance that the Company will successfully develop any product or obtain regulatory approvals, enter clinical trials, achieve other milestones or commercialize any products in accordance with currently anticipated timetables, or at all.

PRODUCT DEVELOPMENT PROGRAMS
AND RESEARCH PROGRAMS

PROGRAM	CELL TYPE(1)	STATUS(2)	PARTNER
		ENCAPSULATED-CELL THERAPIES	
Chronic Pain	Bovine adrenal chromaffin cells	Phase I studies of prototype devices completed in approximately 50 patients; Phase IIA trials initiated to investigate new device version in neuropathic pain patients; mulitcenter placebo controlled Phase IIB trial initiated in pain patients. Enrollment in all trials voluntarily halted to allow modification of implant and device fixation procedures	Astra AB
	Engineered cells releasing analgesics	Research**	Astra AB
Parkinson's Disease	Engineered cells releasing neurotrophic factor(s)	Research**	Genentech, Inc.
Amyotrophic Lateral Sclerosis	Engineered cells releasing human CNTF	Swiss pilot clinical study (investigator+ IND) enrollment completed	
	Engineered cells releasing NT4/5 and CT-1	Research**	Genentech, Inc.*
Huntington's Disease	Engineered cells releasing CNTF	French pilot clinical trial (investigator++ IND) scheduled to begin 2nd quarter of 1998	
	Engineered cells releasing neurotrophic factors	Research**	Genentech, Inc.*
Ophthalmologic Diseases	Engineered cells releasing neurotrophic factor(s), anti-inflammatory(s) and/or antiangiogenic(s)	Research; preliminary rodent experiments completed	
		STEM CELL THERAPIES	
CNS Disorders	Neural stem cells (unencapsulated)	Research/Preclinical Research	
Disorders of the liver and pancreas	Stem cell discovery (unencapsulated)		

(1) All cells are encapsulated unless otherwise indicated.

(2) "Research" refers to early stage research and product development activities IN VITRO, including the selection and characterization of product candidates for preclinical testing.

"Preclinical" refers to further testing of a defined product candidate IN VITRO and in animals prior to clinical studies.

"Pilot clinical study" refers to an initial clinical study in a small number of patients.

* Genentech has commercialization options in these programs; they are funded by CytoTherapeutics.

** Progress in these programs is dependent upon CytoTherapeutics developing an appropriate platform cell(s) for these programs; in particular, the Company is trying to develop hardy cell lines that will survive for appropriately long periods within the Company's capsules.

\+ This trial is being conducted by Dr. Patrick Aebischer; the Company is paying certain costs associated with the trial.

++ This trial is being conducted by a third-party clinical investigator; the Company is paying certain costs associated with the trial.

ENCAPSULATED-CELL THERAPIES--LEAD PROGRAMS

CHRONIC PAIN PROGRAM

The Company estimates that more than one million patients in the United States suffer unrelieved severe, chronic pain. Chronic, intractable pain often accompanies or is the result of a number of serious diseases, procedures and conditions including cancer, infection, nerve damage, back surgery, arthritis, amputation, fractures and other conditions. Even where therapies exist, they often have limits to their effectiveness in treating severe, chronic pain. Patients may become intolerant of or unresponsive to narcotics such as morphine, and may experience undesirable side-effects.

The Company believes that its encapsulated-cell technology can be used to treat chronic pain by implanting encapsulated cells which release naturally occurring analgesic substances, such as catecholamines and opioid peptides. The Company, together with certain of its academic collaborators, has developed methods for the encapsulation of bovine adrenal chromaffin cells for implantation into the lumbar region of the spinal column for the treatment of chronic pain. The Company believes that encapsulating properly chosen cell types which secrete desired therapeutic substances may provide more effective pain relief than traditional approaches and/or may enable treatment of patients who experience little or no relief with other therapies.

During 1993 and 1994, the Company collaborated on a pilot clinical study of its chronic pain implant technology with Dr. Patrick Aebischer, a founding scientist of the Company. The study conducted at the Centre Hospitalier Universitaire Vaudois ("CHUV") in Switzerland included nine seriously or terminally ill patients experiencing severe, intractable pain for whom narcotics, such as morphine, provided inadequate relief or could not be tolerated. The implant procedure was performed safely in all nine patients. Viable implants containing cells were retrieved from eight of the nine patients upon the death of the patient or at or beyond the end of the intended trial period.

In May 1995, the Company commenced its first Company-sponsored Investigational New Drug ("IND") trial in the United States. The Phase I trial was an open label study which included 15 terminally ill cancer patients experiencing severe, intractable pain and having a life expectancy of less than five months. According to the trial protocol, patients were to receive treatment for the remainder of their lives. By February 26, 1997, all 15 patients had completed the study.

In February 1996, the Company initiated an extension of the Phase I trial. In this extension, four patients received a device containing approximately three times the number of cells used in the devices implanted in the first 15 patients. By February 9, 1998, three of the four patients had completed the study. The one patient that remains in the study has had a device in place for nearly two years without any related significant safety issues.

A Phase IIA clinical trial for the treatment of neuropathic pain was then initiated in Switzerland in May 1997. A parallel study was initiated in August 1997 in the United States. These trials were designed to evaluate the safety and retrievability of the larger device. Neuropathic pain patients were implanted with the device for 10 weeks. During the period, patients were monitored for safety and pain scores. Following removal of the original device, patients could elect to be reimplanted for six months.

In addition, in November 1997, a 150-patient, Phase IIB, placebo-controlled, double-blinded, multicenter trial in cancer patients was initiated in central Europe and Switzerland. In this trial, patients with end-stage cancer were and will be implanted with either a cell-containing device or a placebo device for 10 weeks and will be monitored for pain scores, concurrent pain-related drug usage and quality of life. Following removal of the original device, patients can elect to be implanted with an active device for six months.

In December 1997, the Company became aware, after explant of devices from some patients enrolled in the Phase IIA trials, that a significant number of devices had migrated into or out of the intrathecal

space during the evaluation period. In some cases migration resulted in device breakage. To date, there have been no reports of significant medical complications related to device migration or breakage. The Company has investigated this migration phenomenon and has determined that it is necessary to modify the device and the implantation procedure to secure the devices to prevent migration. These modifications have included the development of a "tether clip" to assist in securing the implants. The Company and its partner, Astra Pain Control, have halted accrual in the Phase II trials until the modifications to the implantation procedure can be implemented.

All clinical trials are being conducted by Astra Pain Control.

The Company has been closely monitoring the development of regulatory regimes intended to deal with the risks of xenotransplantation and the use of bovine cells. See "Government Regulations." Although the FDA has proposed guidelines for the conduct of xenotransplantation trials, a number of European countries, for example, have been more restrictive. The FDA has imposed strict and potentially onerous restrictions on the clinical use of non-human cells. These proposed FDA regulations may substantially increase the production costs of implants for the Company's pain program. In addition, such regulations may adversely affect physicians' and patients' perceptions about xenotransplantation. The Company cannot predict the effect of existing regulations or possible future regulatory actions except that, if not modified, they will likely increase the cost of producing pain implants. There can be no assurance that such regulations will not block sales (at least in some countries) or make the product commercially non-viable.

There can be no assurances that the Company will receive regulatory and/or ethical committee approvals to continue the Phase II trials or to initiate other clinical trials in a timely manner or that such clinical trials will be successfully completed or that, if successfully completed, such trials will lead to the commercialization of such product.

In March 1995, the Company entered into a Collaborative Research and Development Agreement with Astra AB for the development and marketing of certain encapsulated-cell products to treat pain. Astra has the right to terminate this Areement anytime after April 1998. See "Corporate Collaborations-- Astra AB."

PARKINSON'S DISEASE PROGRAM

Parkinson's disease ("PD") is a progressively debilitating neurological disorder characterized by tremor, rigidity and reduced spontaneous movement. The symptoms of PD result from inadequate levels of the neurotransmitter dopamine in the striatum (a portion of the brain) due to the death of dopamine-producing cells in the substantia nigra (a related area of the brain). The causes of the disease are unknown. There is no known cure for PD nor is there any known method for arresting or reversing the fundamental neurodegenerative process that results in the death of dopamine-producing cells.

PD affects approximately 500,000 individuals in the United States, and it is estimated that one in 500 people over 50 years of age will develop this disorder. It is thought that approximately 50,000 new cases are diagnosed annually in the United States, and this number is expected to increase as the population ages. The Company's proposed product is expected to initially be targeted for use by the estimated 300,000 mid-to-late-stage PD patients in the United States.

Currently approved therapies for PD generally provide adequate treatment of the disease for a limited period. Patients become increasingly resistant to the benefits of such medications while concurrently becoming susceptible to a variety of motor and cognitive side effects. Under these circumstances, they often require extensive supportive care.

The Company is developing an implant to treat PD. The goal of this program is to slow or prevent progression of the underlying degeneration of dopaminergic neurons by delivering neurotrophic factors to the brain. The initial focus of the program is the delivery of Neurturin, a neurotrophic factor with partial homology to GDNF (glial derived neurotrophic factor), using human cells. The Company believes that, if

successfully developed, its implants will be capable of delivering effective, low doses of Neurturin to the areas of the brain where they are required.

The Company has entered into an agreement with Genentech for the development of implants releasing certain neurotrophic factor(s) to treat PD. Under the terms of this Agreement, if certain development milestones are not achieved before agreed-upon dates, Genentech has the right to terminate the Agreement. See "Corporate Collaborations--Genentech, Inc."

ENCAPSULATED-CELL THERAPIES--OTHER NEURODEGENERATIVE DISEASES

The Company has entered into two additional agreements with Genentech, Inc. under which the Company is attempting to develop encapsulated-cell treatments for ALS and Huntington's disease. The Company has concluded, due to regulatory considerations, that these programs should be based on human cell lines, rather than the xenogeneic cell lines previously envisioned. At the present time, progress in these programs in largely dependent upon the Company's success in identifying human cell lines under its Parkinson's disease program which can survive for appropriately long periods in the encapsulated environment.

ALS PROGRAM

Amyotrophic lateral sclerosis ("ALS"), also known as Lou Gehrig's disease, is characterized by progressive loss of motor control and death due to degeneration of neurons in the motor system. The Company estimates that approximately 25,000 patients have ALS in the United States. The cause of ALS is unknown in most cases. There is no known cure for the disease.

The Company is sponsoring research to evaluate the feasibility and tolerability of using encapsulated human cells to deliver neurotrophic factors into the CNS to treat ALS. Dr. Patrick Aebischer, a scientific founder of the Company, has completed enrollment of an investigator-sponsored, 12-patient, pilot trial of CNTF-releasing encapsulated cells in ALS patients. Results are not yet available.

In November 1996, the Company signed an agreement with Genentech, Inc., for the development and marketing of implants that release NT4/5 and CT-1 (a cytokine related to CNTF) to treat ALS; the Agreement requires certain specific due diligence of the Company (see "Corporate Collaborations-- Genentech, Inc.").

HUNTINGTON'S RESEARCH

Huntington's disease ("HD") is an autosomal dominant, progressive neurodegenerative disease resulting in movement disorders, psychiatric disturbances, and death. The symptoms of HD are caused primarily by the death of striatal neurons. In 1993, there were approximately 25,000 patients with symptomatic HD in the United States. There is no known cure or treatment for the disease.

The Company is sponsoring research to evaluate the feasibility and tolerability of using encapsulated cells to deliver neurotrophic factors into the CNS and to treat HD. An investigator-sponsored trial to treat six Huntington's disease patients has been approved by regulatory authorities in France. The trial, expected to start in the first half of 1998, is intended to test CNTF-releasing encapsulated cells.

In November 1996, CytoTherapeutics entered into an agreement with Genentech, Inc. for the development and marketing of implants that release CT-1 to treat HD; the Agreement requires certain specific due diligence by the Company. See "Corporate Collaborations--Genentech, Inc.".

OPHTHALMOLOGY PROGRAM

Many diseases of the eye are presently ineffectively treated, which can lead to reduced vision and blindness. There are more than one million blind people in the United States and many more Americans

suffer from potentially visually impairing ophthalmologic disorders. The worldwide populations at risk are much larger.

Certain diseases of the eye, e.g., glaucoma and anterior segment inflammation, can be treated today with topical preparations, although the efficacy of these treatments is variable. These disorders are treatable largely because some or all of the disease processes occur in the anterior portion of the eye, which is accessible to topical drugs. Other serious diseases, such as diabetic retinopathy and age-related macular degeneration, are not treatable, in part because they occur in the posterior portion of the eye, an area that is essentially unreachable with most current treatment methods.

Many of these untreatable diseases affect the retina, a posterior part of the eye critical to sight. The retina is part of the CNS and the Company believes that its encapsulated-cell implant technologies can be applied to bypass the blood-retinal barrier of the eye using the same approach as bypassing the blood-brain barrier in the rest of the CNS. If these implants are successfully developed, the Company believes this delivery platform could allow treatment of serious sight-threatening disorders.

CytoTherapeutics has begun design and production of implants adapted for use in the eye and has started initial testing in animals with these implants.

TECHNOLOGY DEVELOPMENT

The Company continues to develop its encapsulated-cell technology. Through its cell biology program, the Company is developing genetically engineered cell lines that will function optimally when encapsulated. The Company's present work focuses on identification of appropriately hardy human cells because of the increasing regulatory constraints on use of non-human cells. There can be no assurance such development will be successful.

The Company is developing cell lines which may represent important components in second generation products (e.g., an engineered cell line to deliver analgesics in its pain program) or new products (such as a single device to deliver multiple therapeutic substances). It is also conducting research to improve cell line expression levels of therapeutic substances, as well as regulation and consistency of output.

The Company continues to evaluate new and modified forms of membranes for use in its implants. These evaluations are focused on developing membranes with increased strength, improved handling characteristics, enhanced transport qualities and greater biocompatibility. These efforts are undertaken internally, as well as externally with Akzo Nobel Faser AG. See "Corporate Collaborations--Akzo Nobel Faser AG."

The Company is also assessing and developing distribution, handling, and insertion systems to facilitate the distribution of its implants to clinicians and enable clinicians both to surgically implant these devices into patients and to retrieve and replace them, as necessary. See "Manufacturing."

STEM CELL THERAPIES

The Company's portfolio of stem cell technology results from the Company's earlier licensing of neural stem/progenitor cell technology the Company's own research and development efforts, and the acquisition of StemCells, Inc. in 1997.

NEURAL STEM/PROGENITOR CELL DEVELOPMENT PROGRAM

The Company began its work with neural stem/progenitor cultures in collaboration with NeuroSpheres, Ltd., in 1992. The Company believes that NeuroSpheres, Ltd., was the first to invent these cultures and NeuroSpheres has filed patent applications on its inventions relating to these cultures. The Company has obtained a license from NeuroSpheres to such inventions for transplantation. See "License Agreements and Sponsored Research Agreements--NeuroSpheres, Ltd."

The Company has in the past and continues today to conduct its own research, as well as sponsoring research, in the area of neural/progenitor cells and their use.

In 1997, Company scientists invented a reproducible method for isolating and growing human neural stem/progenitor cultures. In preclinical IN-VITRO and early IN-VIVO studies, the Company demonstrated that these cells differentiate into all three of the cell types of the CNS. Based on these results, the Company believes that these cells may form the basis for replacement of cells lost in certain degenerative diseases. The Company is continuing research into, and has initiated the development of, its human neural stem/ progenitor cell cultures. The Company has isolated the cultures and demonstrated that these cultures can be expanded for a number of generations IN VITRO in defined media. A collaborator of the Company, Dr. Anders Bjorklund, has shown that these cultures can be successfully engrafted into the brains of rodents. The Company is expanding its preclinical efforts in this area with an initial goal of selecting the proper indications to pursue.

The Company's neural stem/progenitor cell program is at an early stage and there can be no assurance that it will result in any commercial product.

STEM CELL DISCOVERY PROGRAM

The Company, through its 100% owned subsidiary, StemCells, Inc., has begun a program seeking to discover and isolate various stem cells from the human body. The Company believes that stem cells represent a fundamentally new approach to the treatment of diseases caused by lost or damaged tissue. The Company has assembled a very experienced team of scientists and scientific advisors, including Irving L. Weissman, M.D., of Stanford University, Fred H. Gage, Ph.D., of The Salk Institute and David Anderson, Ph.D., of the California Institute of Technology, to search for new stem cells and, in conjunction with a number of academic researchers, has initiated programs for the isolation of the stem cell for the pancreas and the liver. The Company has obtained rights to certain inventions relating to stem cells from, and is conducting stem-cell related research at, several academic institutions. See "License Agreement and Sponsored Research Agreements." The Company expects to expand its search for new stem cells and expects to acquire rights to additional inventions relating to stem cells from third parties.

An important element of the Company's program in stem cell discovery is the development of intellectual property positions with respect to stem and progenitor cells. The Company believes that the first person or entity to isolate and perfect intellectual property rights in new stem/progenitor cells will be able to exclude others from using such cells commercially. To this end the Company, through StemCells, Inc., has entered into several research collaborations with academic institutions.

SUBSIDIARY

STEMCELLS, INC.

On September 26, 1997, CytoTherapeutics acquired by merger StemCells, Inc., a California corporation ("StemCells"). Through the merger, CytoTherapeutics acquired StemCells in exchange for 1,320,691 shares of the Company's common stock and options and warrants for the purchase of 259,296 common shares. Simultaneously with the acquisition of StemCells, Richard M. Rose, M.D., President of StemCells, Inc., became President, Chief Executive Officer and a director of CytoTherapeutics, and Irving L. Weissman, M.D., a founder of StemCells, Inc., became a director of CytoTherapeutics.

The Company's current stem cell research is being conducted pursuant to the provisions of an agreement between CytoTherapeutics and Drs. Weissman and Gage providing for a two-year research plan. If the goals of the research plan are accomplished, the stem cells research will continue to be funded under an extension of such Research Plan approved by a Research Committee consisting of two persons chosen by Drs. Weissman and Gage, two persons chosen by the Company and a fifth member appointed by Drs. Weissman and Gage, subject to the reasonable approval of the Company. Increases in stem cells

research funding of not more than 25% a year approved by the Committee will be funded by CTI for as long as the goals of the Research Plan are being met, provided however, that CTI will retain the option of ceasing or reducing neural stem research even if all of Research Plan goals are being met by accelerating the vesting of all still-achievable performance-based options granted to Drs. Weissman and Gage and other scientists and ceasing or reducing non-neural stem cell research even if all Plan goals are being met by affording StemCells' scientific founders the opportunity to continue development of the non-neural stem research by licensing the technology related to such research to them in exchange for a payment to CytoTherapeutics equal to all funding for such research, plus royalty payments.

CORPORATE COLLABORATIONS

ASTRA AB

In March 1995, the Company signed a collaborative research and development agreement with Astra for the development and marketing of certain encapsulated-cell products to treat pain. Astra made an initial, non-refundable payment of $5,000,000 and may make up to $16,000,000 in additional payments subject to the achievement of certain development milestones. Under the agreement, the Company is obligated to conduct certain research and development pursuant to a four-year research plan agreed upon by the parties. Over the term of the research plan, the Company expects to receive annual research payments from Astra of approximately $5-7 million, which the Company expects should approximate the research and development costs incurred by the Company under the plan. Approximately $29 million of research and development funding has been received by the Company through December 31, 1997. Subject to the successful development of such candidate products and obtaining necessary regulatory approvals, Astra is obligated to fund and to conduct all clinical trials of candidate products arising from the collaboration and to seek approval for their sale and use. Astra has the exclusive worldwide right to market products covered by the agreement. Until the later of either the last to expire of all patents included in the licensed technology or a specified fixed term, the Company is obligated to manufacture and supply products and is entitled to a fixed royalty on the worldwide net sales of such products in return for the license granted to Astra and the supply of product. Astra has the right to terminate the agreement for any reason after April 1, 1998.

As is described in more detail under the caption "Encapsulated-Cell Therapies--Lead Programs-Chronic Pain Program," enrollment in ongoing clinical trials of the Company's implant for the treatment of chronic pain has been voluntarily halted in order to implement modifications to the implantation procedure. There can be no assurance that Astra will continue to fund the research plan under the Agreement after April 1998, or that sufficient modifications to the Company's implant can be made to permit resumption of clinical trials, or that a suitable human cell line can be developed (if necessary because of regulatory considerations) on a timely basis, or at all.

GENENTECH, INC.

On November 25, 1996 the Company entered into three agreements with Genentech, Inc. ("Genentech") to develop treatments for Parkinson's disease, Huntington's disease and amyotrophic lateral sclerosis ("ALS"). Under the agreements the Company and Genentech expect to pursue treatments for these diseases that utilize the Company's encapsulated-cell technology to deliver several of Genentech's neurotrophic factors, potentially including neurotrophin-4/5 ("NT-4/5"), cardiotrophin-1 ("CT-1"), Neurturin and nerve growth factor ("NGF"). These agreements supersede the Development Collaboration and License Agreement between the Company and Genentech entered into in March 1994 which related in part to the development of a product for the treatment of Alzheimer's disease using NGF.

The following is a brief overview of each of the agreements:

PARKINSON'S AGREEMENT

The initial focus of the research under the Development Collaboration and License Agreement relation to Parkinson's disease (the "Parkinson's Agreement") is the development of a treatment for Parkinson's disease using Neurturin. Under the Parkinson's Agreement, the Company is obligated to perform certain preclinical studies and initiate a pilot Phase I clinical study using Neurturin (unless another growth factor is agreed upon by the parties). Genentech purchased $8.3 million of the Company's Common Stock (829,171 shares at $10.01 per share) to fund the Company's expenses associated with such preclinical and pilot clinical studies. If the parties agree that additional funds are required to complete such studies, Genentech will purchase additional shares of the Company's Common Stock (at the then current market price of the Company's Common stock) to provide the Company the additional required funding.

Under the terms of the Agreement signed in 1996, Genentech has the right to terminate development under the Parkinson's Agreement after the completion of each of (i) certain preclinical studies, (ii) the pilot Phase I clinical trial and (iii) a specified Phase II clinical trial. Should Genentech decide to proceed to Phase II clinical trials, Genentech will purchase additional shares of the Company's Common Stock (at the then current market price of the Company's Common Stock) to fund such study. If following completion of the preclinical studies, the pilot clinical study or the Phase II study, Genentech decides to terminate further development under the Parkinson's Agreement or if Genentech terminates the Parkinson's Agreement as a result of a breach of the Parkinson's Agreement by the Company, and the funds the Company received from the sale of stock to Genentech pursuant to the Parkinson's Agreement exceed the expenses incurred by the Company in connection with such studies by more than $1 million, Genentech has the right to require the Company to repurchase from Genentech shares of Company Common Stock having a value equal to the amount of overfunding (based on the per share price at which Genentech purchased such shares of Common Stock from the Company). The Company is obligated to use reasonable efforts to complete its development obligations under the Parkinson's Agreement within prescribed periods. In addition, if certain development milestones are not completed prior to agreed-upon dates, Genentech has the right to terminate the Agreement. The first of these dates may occur as early as May 1998. There can be no assurance that such milestones will be completed in a timely manner or that Genentech will not terminate the Agreement when it is permitted to do so.

In the event Genentech decides to continue with Phase III clinical trials, Genentech and the Company will share the cost of U.S. Phase III clinical trials and Genentech will pay for any clinical testing required to sell products developed under the Parkinson's Agreement outside the United States. Genentech will extend the Company a line of credit to provide the Company cash to fund the Company's share of the expenses of the Phase III trials in the United States. The line of credit, together with interest thereon, is repayable, at the option of the Company, in either cash or through the issuance of shares of the Company's Common Stock having a value (based on the then current market price of the Company's Common Stock) equal to the outstanding amount of the loan.

Upon commercialization, Genentech and the Company will share profits in the United States at an agreed upon percentage, and Genentech will pay the Company a royalty based on sales outside the United States. The Company will retain manufacturing rights and will be paid manufacturing costs for products sold. In the event the Parkinson's Agreement is terminated because of the Company's default or bankruptcy, the Company is required to grant Genentech a license to the Company's cell encapsulation technology and transfer to Genentech related technology for use solely with the products developed under the Parkinson's Agreement.

Under the Parkinson's Agreement, the Company has granted Genentech an exclusive license to use the Company's cell encapsulation technology in certain cases with certain of Genentech's growth factors

for the treatment of Parkinson's disease. Under the Parkinson's Agreement, the Company is also prohibited from entering into certain agreements relating to the development of treatments for Parkinson's disease using certain compounds.

ALS AGREEMENT

Pursuant to the License Agreement between the Company and Genentech Relating to Treatment of Amyotrophic Lateral Sclerosis (the "ALS Agreement") Genentech has granted the Company a license to CT-1 and NT-4/5 to develop products for the treatment of ALS using the Company's cell encapsulation technology. Subject to certain limitations discussed below, the Company is responsible for all expenses associated with the preclinical and clinical development under the ALS Agreement and is obligated to pay Genentech royalties on net sales of products developed under the ALS Agreement. The Company's license to CT-1 and NT-4/5 is dependent upon the Company using reasonable efforts to achieve certain development milestones within prescribed periods.

The Company has the right to commercialize the product outside the United States. Upon the successful completion of a specified Phase II clinical trial, Genentech has the option to obtain exclusive rights to sell products developed under the ALS Agreement in the United States by agreeing to pay an agreed upon percentage of the expenses of United States Phase III clinical development of such products. If Genentech makes such an election, the parties will share profits on sales of such products in the United States, subject to a royalty payable to Genentech. In the event the ALS Agreement is terminated because of the Company's default or bankruptcy, the Company is required to grant Genentech a license to the Company's cell encapsulation technology and to transfer to Genentech-related technology for use solely with the products developed under the ALS Agreement.

HUNTINGTON'S AGREEMENT

Under the License Agreement Relating to Treatment of Huntington's Disease (the "Huntington's Agreement"), Genentech has granted the Company an exclusive license to CT-1 to develop, make, use and sell products for the treatment of Huntington's disease that utilize CT-1 and the Company's cell encapsulation technology. The Company is responsible for all preclinical and clinical development under the Huntington's Agreement, including all expenses associated with such development. The Company will pay Genentech a royalty based on net sales of any products developed under the Huntington's Agreement. The Company's license to CT-1 is dependent upon the Company using reasonable efforts to achieve certain development milestones within prescribed periods.

Upon the earlier of (i) the Company agreeing to grant a third party sublicense rights under the Huntington's Agreement, and (ii) the successful completion of the specified Phase II trial on a product developed under the Huntington's Agreement, Genentech has the option to require the Company to negotiate exclusively with Genentech for a limited period regarding Genentech co-developing and co-marketing products developed under the Huntington's Agreement. In the event the parties are unable to reach an agreement, the Company would have the right to sublicense its rights under the Huntington's Agreement to a third party, provided such third party offers the Company terms more favorable to the Company than the terms of Genentech's last offer. In the event the Huntington's Agreement is terminated because of the Company's default or bankruptcy, the Company is required to grant Genentech a license to the Company's cell encapsulation technology and transfer to Genentech related technology for use solely with products developed under the Huntington's Agreement.

MODEX THERAPEUTIQUES SA

In July 1996, CytoTherapeutics, together with certain founding scientists, established Modex Therapeutiques SA as a Swiss biotherapeutics company to pursue extensions of CytoTherapeutics' broad-based, encapsulated-cell technology for certain applications outside the central nervous system. Modex, headquartered in Lausanne, Switzerland, was formed to integrate technologies developed at three universities

located in Lausanne--the University of Lausanne, the Centre Hospitalier Universitaire Vaudois (CHUV), the Ecole Polytechnique Federale de Lausanne--as well as from the Albert Einstein College of Medicine of Yeshiva University in New York City and CytoTherapeutics--to develop products to treat non-CNS diseases such as diabetes, obesity and anemia. In October 1997, the Company completed a series of transactions which resulted in the establishment of Modex as an independent company in which CytoTherapeutics has an equity position of approximately 25%.

In October 1997, as part of Modex obtaining funds from outside investors, the Company and Modex modified the terms of their existing royalty-bearing Cross License Agreement to (i) expand the field in which Modex is exclusively licensed to apply the Company's encapsulated-cell technology to include, in addition to the original field of diabetes, obesity and anemia, the treatment of hemophilia A and B utilizing Factor VIII and/or Factor IX, and two additional applications to be agreed to by the Company and Modex; (ii) eliminate the requirement to make future milestone payments to Modex of up to 300,000 shares of the Company's Common Stock; (iii) limit the scope of the Company's technology licensed to Modex to existing and future encapsulation technology; and (iv) specify the terms under which the Company will manufacture any products Modex may develop based on the Company's technology and grant Modex an option to manufacture or have manufactured such products on payment of a higher royalty. The Cross License Agreement continues to provide for the payment of royalties from Modex to the Company on the sale of any licensed products. The revised agreement similarly limits the scope of the Modex technology exclusively licensed, on a royalty-bearing basis, to the Company for the application of diseases, conditions and disorders of the central nervous system to existing and future encapsulation technology and to certain additional existing technology.

AKZO NOBEL FASER AG

To develop additional new membranes to be used in the Company's encapsulated-cell products and to obtain access to membrane expertise from one of the world's leading membrane companies, the Company entered into a Development and Supply Agreement with Akzo Nobel Faser AG ("Akzo") dated December 1, 1993. Akzo is the world's largest supplier of medical grade membranes. Under the terms of the agreement, Akzo and the Company are evaluating Akzo's existing membranes to determine if the membranes can be used in connection with the Company's proposed products. In addition, Akzo has begun development of improved membranes for use by the Company. The Company has agreed to reimburse Akzo for a portion of Akzo's costs incurred in the development. In the event the Company determines to use membranes developed by Akzo in the Company's products, Akzo will supply membranes to the Company at Akzo's cost plus a certain profit. Akzo will also be entitled to a royalty on sales of the Company's products utilizing Akzo's membranes. Akzo has agreed not to supply membranes to any other third party for encapsulation of cells for in vivo therapeutic applications. Either Akzo or the Company can terminate the Agreement in the event Akzo is unable or unwilling to supply sufficient quantity of membranes to meet the Company's needs. In such event, Akzo would license the technology necessary to manufacture the membranes to CytoTherapeutics.

The Company has the right to utilize membranes from other manufacturers in its products provided the Company pays a small royalty to Akzo on the sales of such products. The Company will also continue its internal membrane development efforts, and may utilize internally developed membranes in its products without obligation to Akzo.

For the years ending December 31, 1997, 1996 and 1995, the Company paid Akzo under the terms of the agreement approximately $98,000, $295,000 and $118,000, respectively.

SIGNAL PHARMACEUTICALS, INC.

In December 1997, StemCells, Inc. entered into two license agreements with Signal Pharmaceuticals, Inc. under which each party licensed to the other certain patent rights and biological materials for use in

defined fields. The parties are in disagreement as to the interpretation of the rights licensed to StemCells, Inc. The Company cannot presently determine whether this dispute will lead to litigation.

LICENSE AGREEMENTS AND SPONSORED RESEARCH AGREEMENTS

NEUROSPHERES, LTD.

In March 1994, the Company entered into a Contract Research and License Agreement with NeuroSpheres, Ltd. Under the agreement, the Company obtained from NeuroSpheres an exclusive, worldwide, royalty-bearing license for the commercial development and use of certain neural stem cells for transplantation to treat human disease. In 1997, the Company settled a dispute that arose between it and NeuroSpheres, Ltd. under the agreement. Pursuant to the settlement, the Company has obtained an exclusive patent license from NeuroSpheres in the field of transplantation, subject to a limited right of NeuroSpheres to purchase a nonexclusive license from the Company. The Company has developed additional intellectual property relating to the subject matter of the license.

COGNETIX, INC.

In February 1997, CytoTherapeutics, Inc. and Cognetix, Inc. entered into a Collaboration and Development agreement to screen selected peptides isolated by Cognetix for possible development into therapeutic products aimed at a broad range of human disease states using CytoTherapeutics' cell-based delivery technology. The Company and Cognetix are reexamining their relationship; the Company expects this reexamination will lead to termination of the joint project under the agreement signed in February 1997.

The Company and Cognetix have also entered into an option agreement giving CytoTherapeutics the right to option up to three of Cognetix's compounds for use in treating eye diseases. CytoTherapeutics has exercised its right as to one protein.

STATE OF RHODE ISLAND

In 1989, the Company entered into an agreement with the State of Rhode Island pursuant to which an agency of the State reimbursed the Company $1,172,000 for certain research activities the Company funded at Brown University. Under the terms of this grant, the Company is obligated to pay royalties ranging from three to five percent of revenues from products developed under the agreement, to a maximum of $1,758,000.

ACADEMIC RELATIONSHIPS

The Company and its wholly owned subsidiary, StemCells, Inc., have entered into a number of research and/or license agreements with academic organizations. These research agreements provide that the Company will fund certain research costs and in return will have a license or an option for a license to the resulting inventions. Under these license agreements, the Company and/or StemCells, Inc. will typically be subject to obligations of due diligence and the requirement to pay royalties on products which use patented technology licensed under such agreements.

CYTOTHERAPEUTICS, INC.

The Company has expended and expects to continue to expend substantial sums to support academic research programs. To date, the Company's principal academic collaborations have been with Brown University and Dr. Patrick Aebischer at the Centre Hospitalier Universitaire Vaudois in Switzerland. Research and development expenses paid in connection with these collaborations aggregated approximately $1,326,000, $1,337,000 and $1,008,000 for the years ended December 31, 1997, 1996 and 1995, respectively. The Company and StemCells, Inc. also have a number of collaborative relationships with other academic institutions and academic researchers.

StemCells, Inc. has entered into a number of research agreements with academic institutions. These include a Sponsored Research Agreement with The Scripps Research Institute and a Sponsored Research Agreement with Oregon Health Sciences University. These agreements require StemCells, Inc. to fund certain research (in the amounts of approximately $931,000 over three years and $105,000 over one year, respectively) in return for licenses or options to license the inventions resulting from such research.

In addition, StemCells, Inc. has entered into license agreements with the California Institute of Technology and the University of Utah Research Foundation. These license agreements and the agreements referred to in the foregoing paragraph relate largely to stem cells or to progenitor cells and to their isolation and identification.

MANUFACTURING

ENCAPSULATED CELLS

The Company believes the ability to manufacture encapsulated-cell products which are safe and effective will be a key source of competitive advantage in its encapsulated-cell therapy business. Thus, the Company intends to manufacture its proposed products and maintain control of this important proprietary element of its business wherever possible.

The manufacturing process for the Company's lead product (its chronic pain implant) is comprised of five modules: (i) manufacture of the fiber membrane; (ii) assembly of implants; (iii) acquisition and culturing of the cells; (iv) placement of the cells within the implant; and (v) packaging of the cell-loaded implants for shipping to the clinical site. The Company is employing this process, using current Good Manufacturing Practices ("cGMP"), for manufacturing its pain implants for use in clinical trials. Quality control tests are performed on each batch of the finished pain devices to assess sterility and potency. Only batches meeting all specifications are released for use in clinical trials. Critical equipment and processes have been validated to assure manufacturing consistency and control. A 21,000-square foot laboratory and pilot manufacturing facility is now in operation.

Implants for clinical trials are currently produced in small quantities. The commercial-scale manufacture of these products is expected to require specialized automated or semi-automated equipment and expansion of manufacturing facilities. The Company's current manufacturing process has been designed to facilitate the incorporation of additional automation over time.

The facilities and equipment required to manufacture the Company's encapsulated-cell implants are different from those required to manufacture potentially competitive biopharmaceutical products.

The Company's pilot manufacturing plant, without additional expansion or increasing staffing, does not have sufficient capacity to permit the Company to produce all of the products necessary to complete clinical trials in all indications the Company may wish to develop. In addition, the Company has not yet developed the capability to manufacture any of its proposed products on a commercial scale and is unaware of any other company which has manufactured any membrane encapsulated-cell product on a commercial scale. Manufacture of the Company's proposed products is expected to require specialized, automated equipment capable of forming complex polymer membranes into implants which combine media, matrices and living cells, and this process must be carried out on a precisely controlled basis, under sterile conditions in a clean-room environment. Failure to achieve commercial scale manufacturing capability at a reasonable cost or to demonstrate consistent results using manufactured prototypes in preclinical animal studies or clinical trials could prevent or delay submission of products for regulatory approval and initiation of new development programs, which could have a materially adverse effect on the Company. Regulatory restrictions have substantially increased the likely cost of manufacturing a product containing xenogeneic cells for commercial use. Since in certain cases the Company has agreed on pricing for supply of its products before commercial production begins, additional costs of production arising from

regulations or otherwise, may cause the Company's cost of production to exceed the price it receives for producing such products. In addition, fearing liability, certain suppliers of raw materials used by the Company in connection with its implants have or may restrict use of such materials in humans.

There can be no assurance that the Company will be able to develop the capability of manufacturing any of its proposed products on a cost-effective basis, or to identify and contract with manufacturers to produce such products or needed raw materials, at a cost or in the quantities necessary to make a commercially viable product.

STEM CELLS

The keys to successful commercialization of neural stem/progenitor cells include efficacy, safety, consistency of the product and economy of the process. The Company will address these issues by appropriate testing and banking representative vials of large-scale cultures. Commercial production is expected to involve expansion of banked cells and packaging them in an appropriate container(s) after formulating the cells in an effective carrier (which may also be used to affect the stability and engrafting of the stem cells or their progeny). Because of the early stage of the Company's stem/progenitor cell programs, the issues which will affect manufacture of stem/progenitor cell products is relatively unclear.

MARKETING

The Company expects to market and sell its products primarily through co-marketing, licensing or other arrangements with third parties. The Company does not have experience in sales, marketing or distribution and does not expect to develop such capabilities in the near future. Generally, the Company in its commercial arrangements with third parties intends to have the marketing of its products undertaken by its partners, although the Company may seek to retain limited marketing rights in specific markets, particularly where the product may be addressed by a specialty or niche sales force.

PATENTS, PROPRIETARY RIGHTS AND LICENSES

The Company believes that proprietary protection of its inventions will be of major importance to its future business. The Company has a program of vigorously seeking and protecting intellectual property it believes may be useful in connection with its products; the Company believes that its know-how will also provide a significant competitive advantage and intends to continue to develop and protect its know-how. The Company may also, from time to time, seek to acquire licenses to important externally developed technologies.

The Company has exclusive or non-exclusive rights to a portfolio of patents and patent applications related to the encapsulation of cells and related technologies and to various stem cells and methods of deriving and using them. In general, these encapsulation patents and patent applications pertain to the release of neurotransmitters from encapsulated cells, use of various cell types, encapsulation devices and their manufacture, encapsulation methods and various aspects of the therapeutic use of capsules in the treatment of various diseases. The stem/progenitor cell patents and patent applications relate mainly to compositions of matter, methods of obtaining such cells, and methods for preparing and utilizing such cells. Currently, the Company's U.S. patent portfolio includes rights to 36 issued U.S. patents and a number of pending patent applications.

The patent positions of pharmaceutical and biotechnology companies, including those of the Company, are uncertain and involve complex and evolving legal and factual questions. The coverage sought in a patent application can be denied or significantly reduced before or after the patent is issued. Consequently, the Company does not know whether any of its pending applications will result in the issuance of patents, or if any existing or future patents will provide significant protection or commercial advantage or will be circumvented by others. Since patent applications are secret until patents are issued in the United States or the applications are published in foreign countries, and since publication of discoveries in the scientific or

patent literature often lags behind actual discoveries, the Company cannot be certain that it was the first to make the inventions covered by each of its pending patent applications or that it was the first to file patent applications for such inventions. There can be no assurance that patents will issue from the Company's pending or future patent applications or, if issued, that such patents will be of commercial benefit to the Company, afford the Company adequate protection from competing products or not be challenged or declared invalid.

In the event that a third party has also filed a patent application relating to inventions claimed in Company patent applications, the Company may have to participate in interference proceedings declared by the United States Patent and Trademark Office to determine priority of invention, which could result in substantial uncertainties and cost for the Company, even if the eventual outcome is favorable to the Company. There can be no assurance that the Company's patents, if issued, would be held valid by a court of competent jurisdiction.

A number of pharmaceutical, biotechnology and other companies, universities and research institutions have filed patent applications or have been issued patents relating to cell therapy and encapsulation, stem cells and other technologies potentially relevant to or required by the Company's expected products. In particular, a third party has received a U.S. patent which such third party asserts relates to cells for alleviating chronic pain in humans. The Company cannot predict which, if any, of such applications will issue as patents or the claims which might be allowed. The Company is aware that a number of companies have filed applications relating to stem cells. The Company is also aware of a number of patent applications and patents claiming use of genetically modified cells to treat disease, disorder or injury. The Company also cannot predict the impact of the application of existing patent applications and patents on future unencapsulated products. The Company is aware of two issued patents to a competitor claiming certain methods for treating defective, diseased or damaged cells in the mammalian CNS by grafting genetically modified donor cells from the same mammalian species. The Company is also aware of third party patents and patent applications claiming rights to the neurotrophic factors which the Company hopes to deliver with its cell encapsulation technology, and to the production of these factors through the use of genetically modified cells. The Company expects to use genetically modified cells to produce these factors for use in its products.

The Company may also be required to seek licenses in regard to other cell lines, the techniques used in creating or obtaining such cell lines, growth factors required to obtain and maintain such cell lines, the materials used in the manufacture of its implants or otherwise. If third party patents or patent applications contain claims infringed by the Company's technology and such claims or claims in issued patents are ultimately determined to be valid, there can be no assurance that the Company would be able to obtain licenses to these patents at a reasonable cost, if at all, or be able to develop or obtain alternative technology. If the Company is unable to obtain such licenses at a reasonable cost, it may be adversely affected. There can be no assurance that the Company will not be obliged to defend itself in court against allegations of infringement of third-party patents. Patent litigation is very expensive and could consume substantial resources and create significant uncertainties. An adverse outcome in such a suit could subject the Company to significant liabilities to third parties, require disputed rights to be licensed from third parties, or require the Company to cease using such technology.

The Company also relies upon trade-secret protection for its confidential and proprietary information. There can be no assurance that others will not independently develop substantially equivalent proprietary information or techniques, gain access to the Company's trade secrets or disclose such technology, or that the Company can meaningfully protect its trade secrets.

The Company's policy is to require its employees, consultants, significant scientific collaborators and sponsored researchers to execute confidentiality agreements upon the commencement of an employment or consulting relationship with the Company. These agreements generally provide that all confidential information developed or made known to the individual by the Company during the course of the

individual's relationship with the Company is to be kept confidential and not disclosed to third parties except in specific circumstances. In the case of employees and consultants, the agreements generally provide that all inventions conceived by the individual in the course of rendering services to the Company shall be the exclusive property of the Company. There can be no assurance, however, that these agreements will provide meaningful protection or adequate remedies for the Company in the event of unauthorized use, transfer or disclosure of such information or inventions.

The Company has obtained rights from universities and research institutions to technologies, processes and compounds that it believes may be important to the development of its products. These agreements typically require the Company to pay license fees, meet certain diligence obligations and, upon commercial introduction of certain products, pay royalties. These include exclusive license agreements with Brown University and NeuroSpheres, Ltd. to certain patents and know-how regarding present and certain future developments in encapsulation technology and neural stem cells, respectively. The Company's licenses may be canceled or converted to non-exclusive licenses if the Company fails to use the relevant technology or the Company breaches its agreement. Loss of such licenses could expose the Company to the risks of third party patents and/or technology. There can be no assurance that any of these licenses will provide effective protection against the Company's competitors.

COMPETITION

The Company's initial products are expected to compete with a variety of therapeutic products and procedures. Major pharmaceutical companies currently offer a number of pharmaceutical products to treat chronic pain, Parkinson's disease, and other diseases for which the Company's technologies may be applicable. The Company believes that its products, if successfully developed, will compete with these products principally on the basis of improved and extended efficacy and safety and the overall economic benefit to the health care system offered by such products. However, many pharmaceutical and biotechnology companies are investigating new drugs and therapeutic approaches to treat neurodegenerative diseases, which may achieve new and better efficacy profiles, extend the therapeutic window, alter the prognosis of these diseases or prevent their onset.

The market for therapeutic products that address degenerative diseases is large, and competition is intense and is expected to increase. The Company's most significant competitors are expected to be fully integrated pharmaceutical companies and more established biotechnology companies. Such competitors have significant resources and expertise in research and development, manufacturing, testing, obtaining regulatory approvals and marketing and also have significantly greater capital resources. Smaller companies may also prove to be significant competitors, particularly through collaborative arrangements with large pharmaceutical or biotechnology companies. Many of these competitors have significant products approved or in development which could be competitive with the Company's potential products, and also operate large, well-funded research and development programs. In addition, the Company competes with other companies and institutions for highly qualified scientific and management personnel.

The Company's products to treat chronic pain, if successfully developed, will compete with epidural and intrathecal opiates, such as morphine and its analogs, and with adjuvant analgesics, antidepressants and anticonvulsants, as well as with new therapeutics under development such as SNX 111, a conopeptide. New delivery and dose control methods for traditional pain treatments, such as morphine pumps, may also compete with the Company's products.

The Company's products to treat Parkinson's disease, if successfully developed, may compete with orally administered drugs which contain L-dopa, other forms of cell transplantation, ablative and stimulative procedures and new drugs under development. Neurotrophic factors delivered to the patient other than with the Company's encapsulation technology, such as by gene therapy, also represent potential products that may compete with the Company's products. In addition, certain companies are attempting to

develop gene therapies including products (which may or may not involve neurotrophic factors) for the treatment of a number of neurodegenerative diseases, including Parkinson's disease.

The Company's stem/progenitor cell products, if successfully developed, might face competition from existing products like those referred to in the preceding paragraph. In addition, the Company believes that its competitors are trying to develop stem/progenitor cell-based technologies. The Company expects that these products, if developed, will compete with the Company's potential stem/progenitor cell products based on efficacy, safety, cost and intellectual property positions. The Company expects that gene therapy, if successfully developed, will also be a source of competition for potential stem/progenitor cell products.

There can be no assurance that the Company's competitors will not succeed in developing technologies and products that are more effective than those being developed by the Company or that would render the Company's technology obsolete or non-competitive. The Company may also face competition from companies which have filed patent applications relating to cell encapsulation and the use of genetically modified cells to treat disease, disorder or injury. The Company may be required to seek licenses from these competitors in order to commercialize certain of its proposed products and there can be no assurance that the Company will be able to obtain such licenses at a reasonable cost, if at all.

Any product that the Company succeeds in developing and for which it gains regulatory approval must then compete for market acceptance and market share. For certain of the Company's potential products, an important competitive factor will be the timing of market introduction of competitive products. Accordingly, the Company expects that an important competitive factor will be the relative speed with which the Company and its competitors can develop products, complete the clinical testing and approval processes and supply commercial quantities of a product to market. With respect to clinical testing, competition may delay progress by limiting the number of clinical investigators and patients available to test the Company's potential products.

Competition for the Company's products is also expected to be based on product efficacy, safety, the timing and scope of regulatory approvals including, in certain instances, obtaining marketing exclusivity under the Orphan Drug Act, availability of supply, marketing and sales capability, reimbursement coverage, price and patent and technology position. There can be no assurance that the Company's technology, if fully developed, will become commercially viable.

GOVERNMENT REGULATION

The manufacturing and marketing of the Company's potential products and its research and development activities are and will continue to be subject to regulation for safety and efficacy by numerous governmental authorities in the United States and other countries. In the United States, pharmaceuticals, biologicals and medical devices are subject to rigorous FDA regulation. The Federal Food, Drug and Cosmetic Act, as amended, and the Public Health Service Act, as amended, the regulations promulgated thereunder, and other Federal and state statutes and regulations govern, among other things, the testing, manufacture, safety, efficacy, labeling, storage, export, record keeping, approval, marketing, advertising and promotion of the Company's potential products. Product development and approval within this regulatory framework takes a number of years and involves substantial uncertainty combined with the expenditure of substantial resources. In addition, the United States, states and other jurisdictions have restrictions on the use of fetal tissue which could restrict the Company's use of such materials.

Three branches of the FDA, the Center for Drug Evaluation and Research, the Center for Biologics Evaluation and Research and the Center for Devices and Radiological Health, review and approve drugs, biologics and devices, respectively. The FDA has indicated to the Company that the Center for Biologics Evaluation and Research will have primary jurisdiction for premarket review of the Company's potential products that utilize the Company's encapsulated-cell technology. However, the FDA has also indicated that the Center for Drug Evaluation and Research and the Center for Devices and Radiological Health will play a role in the agency's review of the Company's potential products. In addition, the FDA has

published certain guidelines regarding living cells and their transplantation and has begun to develop guidelines for the regulation of xenotransplantation of cells and organs.

The steps required before the Company's potential products may be marketed in the United States include (i) preclinical laboratory and animal tests, (ii) the submission to the FDA of an application for an Investigational New Drug Exemption ("IND"), which must become effective before U.S. human clinical trials may commence, (iii) adequate and well-controlled human clinical trials to establish the safety and efficacy of the product, (iv) the submission to the FDA of a marketing authorization application(s) and (v) FDA approval of the application(s) prior to any commercial sale or shipment of the drug. Biologic product manufacturing establishments located in certain states also may be subject to separate regulatory and licensing requirements.

Preclinical tests include laboratory evaluation of the product and animal studies to assess the potential safety and efficacy of the product and its formulation as well as the quality and consistency of the manufacturing process. The results of the preclinical tests are submitted to the FDA as part of an IND, and the IND becomes effective 30 days following its receipt by the FDA, absent questions, requests for delay or objections from the FDA.

Clinical trials involve the evaluation of the product in healthy volunteers or in patients under the supervision of a qualified principal physician. Clinical trials are conducted in accordance with protocols that detail the objectives of the study, the parameters to be used to monitor safety and the efficacy criteria to be evaluated. Any product administered in a U.S. clinical trial must be manufactured in accordance with cGMP. Each protocol is submitted to the FDA as part of the IND. The protocol for each clinical study must be approved by an independent Institutional Review Board ("IRB") at the institution at which the study is conducted and the informed consent of all participants must be obtained. The IRB will consider, among other things, the existing information on the product, ethical factors, the safety of human subjects, the potential benefits of therapy and the possible liability of the institution.

Clinical development is traditionally conducted in three sequential phases. The phases may overlap, however. In Phase I, products are typically introduced into healthy human subjects or into selected patient populations to test for safety (adverse reactions), dosage tolerance, absorption and distribution, metabolism, excretion and clinical pharmacology. Phase II involves studies in a limited patient population to (i) determine the efficacy of the product for specific targeted indications and populations, (ii) determine optimal dosage and dosage tolerance and (iii) identify possible adverse effects and safety risks. When a dose is chosen and a candidate product is found to be effective and to have an acceptable safety profile in Phase II evaluations, Phase III trials are undertaken to conclusively demonstrate clinical efficacy and to test further for safety within an expanded patient population, generally at multiple study sites. In certain instances, as may be the case with the Company's potential products, the FDA permits Phase I clinical trials to be conducted using a small number of patients instead of healthy volunteers. The FDA continually reviews the clinical trial plans and results and may suggest changes or may require discontinuance of the trials at any time if significant safety issues arise. The results of the preclinical studies and clinical studies are submitted to the FDA in the form of a marketing approval authorization application.

The testing and approval process is likely to require substantial time, effort and expense and there can be no assurance that any FDA approval will be granted on a timely basis, if at all. The time to approval is affected by a number of factors, including relative risks and benefits demonstrated in clinical trials, the availability of alternative treatments and the severity of the disease. Additional animal studies or clinical trials may be requested during the FDA review period and may delay marketing approval. After FDA approval for the initial indications and requisite approval of the manufacturing facility, further clinical trials may be necessary to gain approval for the use of the product for additional indications. The FDA may also require unusual or restrictive post-marketing testing and surveillance to monitor for adverse effects, which can involve significant expense or grant only conditional approvals.

Among the conditions for product licensure is the requirement that the prospective manufacturer's quality control and manufacturing procedures conform to cGMP. Even after product licensure approval, the manufacturer must comply with cGMP on a continuing basis, and what constitutes cGMP may change as the state of the art of manufacturing changes. Domestic manufacturing facilities are subject to regular FDA inspections for cGMP compliance (normally at least every two years), and foreign manufacturing facilities are subject to periodic FDA inspections or inspections by the foreign regulatory authorities with reciprocal inspection agreements with the FDA. Domestic manufacturing facilities may also be subject to inspection by foreign authorities.

The Orphan Drug Act provides incentives to drug manufacturers to develop and manufacture drugs for the treatment of diseases or conditions that affect fewer than 200,000 individuals in the United States. Orphan drug status can also be sought for treatments for diseases or conditions that affect more than 200,000 individuals in the United States if the sponsor does not realistically anticipate its product becoming profitable from sales in the United States. The Company may apply for orphan drug status for certain of its therapies. Under the Orphan Drug Act, a manufacturer of a designated orphan product can seek tax benefits, and the holder of the first FDA approval of a designated orphan product will be granted a seven-year period of marketing exclusivity in the United States for that product for the orphan indication. While the marketing exclusivity of an orphan drug would prevent other sponsors from obtaining approval of the same compound for the same indication, it would not prevent other types of products from being approved for the same use including in some cases, slight variations on the originally designated orphan product. Legislation has been introduced in the U.S. Congress in the past, and is likely to be introduced again in the future, that would restrict the extent and duration of the market exclusivity of an orphan drug, and there can be no assurance that the benefits of the existing statute will remain in effect.

Export of the Company's investigational products is governed by laws and regulations administered by the FDA. The Company has sought and received FDA clearance for export of finished products for clinical trials outside the United States. However, both the Company's past and future export practices could be subject to FDA challenge and there can be no assurance that the FDA would agree that such practices are in compliance with applicable law and regulations or that such exports would be allowed.

Proposed regulations of the FDA and other governmental agencies would place restrictions, including disclosure requirements, on researchers who have a financial interest in the outcome of their research. Under the proposed regulations, the FDA could also apply heightened scrutiny to, or exclude the results of, studies conducted by such researchers when reviewing applications to the FDA which contain such research. Certain of the Company's collaborators have stock options or other equity interests in the Company that could subject such collaborators and the Company to the proposed regulations.

There has been increasing regulatory concern about the risks of xenotransplantation. Concern has focused on the use of cells derived from cows (such as are used in the Company's pain program) and cells from primates and pigs. The United Kingdom has adopted a moratorium on xenotransplantation pending further research and discussion; the EC Commission has introduced a ban on the use of "high-risk material" from cattle and sheep in the Member States of the European Union in the manufacture of pharmaceuticals (this ban would apparently not include the type of cells used in the Company's pain program). In addition, the FDA has recently proposed guidelines which impose significant constraints on the clinical use of non-human cells. The regulations proposed, particularly if they are made more restrictive, could impact significantly on the cost of clinical trials and the cost to manufacture products using xenogeneic cells; the Company has begun to concentrate on the use of human cells as opposed to cells derived from non-human animals. Furthermore, the FDA has published a "Proposed Approach to Regulation of Cellular and Tissue-Based Products" which relates to the use of human cells. The Company cannot presently determine the effects of such actions nor what other actions might be taken. Restrictions on the testing or use of cells, whether human or nonhuman, as human therapeutics could adversely affect the Company's product development programs and the Company itself and could prevent the Company

from producing and/or selling certain products or make the cost of production by the Company prohibitively high.

In addition to safety regulations enforced by the FDA, the Company is also subject to regulations under the Occupational Safety and Health Act, the Environmental Protection Act, the Toxic Substances Control Act and other present and potential future supranational, foreign, Federal, state and local regulations.

Outside the United States, the Company will be subject to regulations which govern the import of drug and device products from the United States or other manufacturing sites and foreign regulatory requirements governing human clinical trials and marketing approval for its products. The requirements governing the conduct of clinical trials, product licensing, pricing and reimbursements vary widely from country to country. In particular, the European Union ("EU") is revising its regulatory approach to high tech products and representatives from the United States, Japan and the EU are in the process or harmonizing and making more uniform the regulations for the registration of pharmaceutical products in these three markets. Although certain of such proposals have been adopted, the Company cannot anticipate what effect the adoption of the final forms of this harmonization or the changes to the EU high tech procedure may have.

Switzerland is expected to conduct a referendum in 1998 to determine the extent to which the use of recombinant DNA technologies may be restricted within Switzerland. The Company cannot predict the results of the referendum or determine the effects of such restrictions.

REIMBURSEMENT AND HEALTH CARE COST CONTROL

The Company's ability to commercialize products successfully may depend in part on the extent to which reimbursement for the costs of such products and related treatments will be available from government health administration authorities, private health insurers and others both in the United States and abroad. Significant uncertainty exists as to the reimbursement status of newly approved health care products. Reimbursement limitations or prohibitions with respect to any product developed by the Company could adversely affect the Company's ability to establish and maintain price levels sufficient for realization of an appropriate return on its investment in developing new therapies. Government and other third party payers are increasingly attempting to contain health care costs by limiting both coverage and the level of reimbursement for new therapeutic products approved for marketing by the FDA and by refusing, in some cases, to provide any coverage for uses of approved products for disease indications for which the FDA has not granted marketing approval. If adequate coverage and reimbursement levels are not provided by third party payers for uses of the Company's therapeutic products, the market acceptance of these products would be adversely affected.

The revenues and profitability of health care-related companies may be affected by the continuing efforts of governmental and third party payers to contain or reduce the cost of healthcare through various means. For example, in certain foreign markets pricing or profitability of prescription pharmaceuticals is subject to government control. In the United States, there have been, and the Company expects that there will continue to be, a number of Federal and state proposals to implement government control over healthcare costs. Efforts at healthcare reform are likely to continue in future legislative sessions. It is uncertain what legislative proposals will be adopted or what actions Federal, state or private payers for healthcare goods and services may take in response to healthcare reform proposals of legislation. The Company cannot predict the effect healthcare reforms may have on its business. Any such reforms as well as the uncertainty their proposal engenders could have a material adverse effect on the Company.

EMPLOYEES

As of March 9, 1998, the Company had 120 full-time employees, including 20 employees with Ph.D. or M.D. degrees. Approximately 101 employees work in research and development, regulatory affairs,

prototype manufacturing, quality assurance and control and laboratory support services. A number of the Company's employees have held positions with other biotechnology or pharmaceutical companies or have worked in university research programs. No employees are covered by collective bargaining agreements.

SCIENTIFIC ADVISORY BOARD

Members of the Company's Scientific Advisory Board provide the Company with strategic guidance in regard to its research and product development programs, as well as assistance in recruiting employees and collaborators. Each Scientific Advisory Board member has entered into a consulting agreement with the Company. These consulting agreements typically specify the compensation to be paid to the consultant and require that all information about the Company's products and technology be kept confidential. All of the Scientific Advisory Board members are employed by employers other than the Company and may have commitments to or consulting or advising agreements with other entities which may limit their availability to the Company. The Scientific Advisory Board members have generally agreed, however, for so long as they serve as consultants to the Company, not to provide any services to any other entities which would conflict with the services the member provides to the Company. Members of the Scientific Advisory Board offer consultation on specific issues encountered by the Company as well as general advice on the directions of appropriate scientific inquiry for the Company. In addition, certain Scientific Advisory Board members assist the Company in assessing the appropriateness of moving the Company's projects to more advanced stages. The following persons are members of the Company's Scientific Advisory Board:

IRVING L. WEISSMAN, M.D., is the Karel and Avice Beekhuis Professor of Cancer Biology, Professor of Pathology and Professor of Developmental Biology at Stanford University. Dr. Weissman is a cofounder of Systemix, Inc., and Chairman of the Scientific Advisory Board of Systemix, Inc. He has served on the Scientific Advisory Boards of Amgen Inc., DNAX and T-Cell Sciences, Inc. Dr. Weissman is Chairman of the Scientific Advisory Board of CytoTherapeutics.

PATRICK AEBISCHER, M.D., PH.D., is the Director of the Gene Therapy Center at the Centre Hospitalier Universitaire Vaudois, Lausanne, Switzerland and Professor of Biomaterials, Brown University. He is also Professor of the Swiss Polytechnical School in Lausanne. Dr. Aebischer is a founding scientist of the Company and a member of its Board of Directors and Chairman of the Board of Modex Therapeutiques SA.

DAVID J. ANDERSON, PH.D., is Professor of Biology, California Institute of Technology, Pasadena, California and Investigator, Howard Hughes Medical Institute.

ANDERS BJORKLUND, M.D., is Professor, University of Lund, Lund, Sweden.

CONSTANCE L. CEPKO, PH.D., is Professor, Department of Genetics, Harvard Medical School, Boston, Massachusetts.

FRED H. GAGE, PH.D., is Professor, Laboratory of Genetics, The Salk Institute for Biological Studies, La Jolla, California and Adjunct Professor, Department of Neurosciences, University of California, San Diego, California.

WILLIAM F. HICKEY, M.D., is Chairman of Pathology, Dartmouth-Hitchcock Medical Center, Lebanon, New Hampshire.

SIR PETER J. MORRIS, PH.D., is Professor, Nuffield Department of Surgery, Oxford University, Oxford, England.

MEDICAL ADVISORY BOARD

The Company is creating a Medical Advisory Board to advise the Company on the clinical aspects of its projects, including the indications to be pursued and the trial strategies that are most efficient and effective. Edwin Cadman, M.D., Chief of Staff, Yale-New Haven Hospital and former Chairman of Abbott

Laboratories Medical Advisory Board, has agreed to assist the Company in establishing the Board and to be its Chairman.

ITEM 2. PROPERTIES

The Company's research laboratories and administrative offices are located in a 65,000 square-foot multipurpose building housing wet labs, specialty research areas and administrative offices located in Lincoln, RI. The facilities are leased pursuant to a fifteen-year lease agreement with the Company having certain renewal options. The Company has also leased a 21,000 square-foot pilot manufacturing facility and a 3,000 square-foot cell processing facility for its pain program in Lincoln, Rhode Island. This facility was financed by bonds issued by the Rhode Island Industrial Facilities Corporation. The Company has also leased additional space near its pilot plant for expanded research and development. In 1998, the Company entered into a three-year lease for approximately 6,000 square feet of laboratory space in Sunnyvale, California. This space is being refitted to serve as the laboratory for the research activities of the Company's subsidiary, StemCells, Inc.

The Company's current facilities are expected to be sufficient to accommodate the Company's needs at least past the end of 1999.

ITEM 3. LEGAL PROCEEDINGS

None.

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

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDERS MATTERS

The Common Stock of CytoTherapeutics is traded on the National Market System of NASDAQ under the Symbol CTII. The quarterly ranges of high and low sales prices since January 1, 1996 are shown below:

1998	HIGH	LOW
First Quarter (through March 12)	$ 4 3/16	$ 2 9/16

1997	HIGH	LOW
Fourth Quarter	$ 7 1/8	$ 3 11/16
Third Quarter	$ 6 1/8	$ 4 3/4
Second Quarter	$ 8 3/4	$ 4 15/16
First Quarter	$10 7/8	$ 8 3/8

1996	HIGH	LOW
Fourth Quarter	$11	$ 7 5/8
Third Quarter	$12 5/8	$ 7 1/8
Second Quarter	$15 1/2	$10 5/8
First Quarter	$18 3/4	$12 3/4

No cash dividends have been declared on the Common Stock since the Company's inception.

As of March 9, 1998, there were approximately 268 holders of record of the Common Stock.

On December 11, 1996, the Company sold 829,171 shares of Common Stock to Genentech in connection with the Company's collaboration agreement with Genentech for $10.01 per share. The shares were issued as a transaction exempt from registration pursuant to Section 4(2) of the Securities Act of 1933 based on, among other things, availability of information about the issuer and representations by the purchaser as to sophistication.

ITEM 6. SELECTED FINANCIAL DATA

	YEAR ENDED DECEMBER 31,				
	1997	1996	1995	1994	1993
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)				
STATEMENT OF OPERATIONS DATA					
Revenue from collaborative agreements	$ 10,617	$ 7,104	$ 11,761	$ 1,250	$ 190
Research and development expenses	18,604	17,130	14,730	13,514	11,807
Acquired research and development	8,344	--	--	--	--
Net loss	(18,114)	(13,759)	(8,891)	(16,461)	(12,544)
Net loss per share(1)	(1.08)	(0.89)	(0.69)	(1.52)	(1.47)
Shares used in computing net loss per share(1)	16,704	15,430	12,799	10,833	8,541

	DECEMBER 31,				
	1997	1996	1995	1994	1993
	(IN THOUSANDS)				
BALANCE SHEET DATA					
Cash and cash equivalents and marketable securities	$ 29,050	$ 42,607	$ 44,192	$ 19,138	$ 30,855
Total assets	44,301	58,397	56,808	32,194	40,996
Long-term debt, including capitalized leases	4,108	8,223	5,441	5,641	3,428
Redeemable common stock	5,583	8,159	--	--	--
Stockholders' equity	28,900	34,747	45,391	22,637	34,509

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(1) See Note 2 to consolidated financial statements.

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

The following discussion of the financial condition and results of operations of CytoTherapeutics, Inc. should be read in conjunction with the accompanying financial statements and the related footnotes thereto.

OVERVIEW

Since its inception in August 1988, the Company has been primarily engaged in research and development of human therapeutic products. No revenues have been derived from the sale of any products, and the Company does not expect to receive revenues from product sales for at least several years. The Company expects that its research and development expenditures will increase substantially in future years as research and product development efforts accelerate and clinical trials are initiated or broadened. The Company has incurred annual operating losses since inception and expects to incur substantial operating losses in the future. As a result, the Company is dependent upon external financing from equity and debt offerings and revenues from collaborative research arrangements with corporate sponsors to finance its operations. The Company's results of operations have varied significantly from year to year and quarter to quarter and may vary significantly in the future due to the occurrence of material, non recurring events, including without limitation, the receipt of one-time, non recurring licensing payments.

RESULTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 1997, 1996 AND 1995

Revenues from collaborative agreements totaled $10,617,000, $7,104,000 and $11,761,000 for the years ending December 31, 1997, 1996 and 1995, respectively. Revenues were earned primarily from a Development, Marketing and License Agreement with Astra AB, which was signed in March 1995. Included in the 1997 revenue is a $3,000,000 milestone payment from Astra AB related to the Phase II clinical program for the Company's pain control implant. Included in 1995 revenue is a one-time licensing fee from Astra AB of $5,000,000.

Research and development expenses totaled $18,604,000 in 1997, as compared to $17,130,000 in 1996 and $14,730,000 in 1995. The increase of $1,474,000, or 9% from 1996 to 1997 was primarily attributable to an increase in manufacturing supplies associated with Phase II clinical trials and an additional $917,000 of expense from Modex Therapeutiques SA ("Modex") the Company's formerly 50% owned subsidiary, which was included in CytoTherapeutics' operating results through October 1997. The increase of $2,400,000, or 16% from 1995 to 1996 was primarily attributable to increases in the number of research, development and production staff, spending for company sponsored research at academic and other institutions and scientific consulting.

Acquired research and development consists of a one-time charge of $8,344,000 related to the acquisition of StemCells, Inc. Commercialization of the acquired technology will require significant incremental research expenditures over a number of years.

General and administrative expenses were $6,158,000 for the year ended December 31, 1997, compared with $5,679,000 in 1996 and $4,620,000 in 1995. The increase of $479,000 , or 8%, from 1996 to 1997 was primarily attributable to increased spending for legal fees associated with the NeuroSpheres, Ltd. arbitration, patents, recruiting fees and other professional services. The increase of $1,059,000, or 23%, from 1995 to 1996 was principally due to increases in the number of administrative personnel, one-time hiring bonuses, as well as consulting costs attributable to the establishment of Modex, a formerly 50% owned Swiss subsidiary.

Interest income for the years ended December 31, 1997, 1996 and 1995 totaled $1,931,000, $2,260,000 and $1,714,000, respectively. The average cash and investment balances were $33,343,000, $37,600,000 and

$26,907,000 in 1997, 1996 and 1995, respectively. The decrease in interest income from 1996 to 1997 was attributable to lower average balances. The increase in interest income from 1995 to 1996 was principally due to higher average balances.

In 1997, interest expense was $438,000, compared with $618,000 in 1996 and $685,000 in 1995. The decrease from 1996 to 1997 was attributable to capitalization of interest on the new facility in the amount of $210,000. The decrease in 1995 to 1996 is principally due to decreasing balances of capitalized lease obligations only partially offset by additional collateralized loan obligations.

In October 1997, the Company recognized a gain in the amount of $3,387,000 related to the sale of half of the Company's interest in Modex.

In December 1995, the Company recognized a loss on its investment in Neocrin Company of $2,330,848, as it determined that the carrying value in its investment had been permanently impaired. The valuation reserve of $2,330,848 reduced the valuation of the investment to $200,000.

The net loss in 1997, 1996 and 1995 was $18,114,000, $13,759,000, and $8,891,000, respectively. The loss per share was $1.08, $0.89 and $0.69 in 1997, 1996 and 1995, respectively. The large increase in 1997 is attributable to a one-time charge of $8,344,000 for acquired research and development related to the purchase of StemCells, Inc. offset by a gain on partial sale of the Company's interest in Modex Therapeutiques, SA in the amount of $3,387,000. The decreased loss in 1996 and 1995 is principally due to revenue earned for research funding under the Company's agreement with Astra AB.

LIQUIDITY AND CAPITAL RESOURCES

Since its inception, the Company has financed its operations through the sale of common and preferred stock, the issuance of long-term debt and capitalized lease obligations, revenues from collaborative agreements, research grants and interest income.

The Company had unrestricted cash, cash equivalents and marketable securities totaling $29,050,000 at December 31, 1997. Cash equivalents and marketable securities are invested in agencies of the U.S. government, investment grade corporate bonds and money market funds.

In May 1996, the Company secured an equipment loan facility with a bank in the amount of $2,000,000. The Company has borrowed $741,000 under this agreement as of December 31, 1997. The loan requires interest payments only for the first two years; principal payments are payable over a three-year period beginning May 1998. Any unused commitment expires on May 15, 1998. The loan is secured by equipment purchased with the proceeds of the credit facility.

In October 1997, the Company completed a series of transactions which resulted in the establishment of its previously 50%-owned Swiss subsidiary, Modex as an independent company. In the transactions, the Company reduced its ownership interest from 50% to approximately 25% in exchange for $4 million cash and elimination of its prior contingent obligation to contribute an additional Sfr 2.4 million (approximately $1.7 million) to Modex in July 1998. In the transactions, all of the put and call arrangements between the Company and other stockholders of Modex were eliminated and the Company forgave $463,000 due from Modex Therapeutiques, SA, to the Company. The Company recorded a gain on the transaction of $3,387,000 and will account for its now 25% ownership interest under the equity method.

The Company and Modex also modified the terms of their existing royalty-bearing Cross License Agreement to (i) expand the field in which Modex is exclusively licensed to apply the Company's proprietary encapsulated cell technology to include, in addition to the original field of diabetes, obesity and anemia, the treatment of hemophilia A and B utilizing Factor VIII and/or Factor IX and two additional applications to be agreed to by the Company and Modex (ii) eliminate the requirement to make future milestone payments to Modex of up to 300,000 shares of the Company's Common Stock; (iii) limit the scope of the Company's technology licensed to Modex to existing and future encapsulation technology; and

(iv) specify the terms under which the Company will manufacture any products Modex may develop based on the Company's technology and grant Modex an option to manufacture or have manufactured such products on payment of a higher royalty. The Cross License Agreement continues to provide for the payment of royalties from Modex to the Company on the sale of any licensed products. The revised agreement similarly limits the scope of the Modex technology exclusively licensed, on a royalty-bearing basis, to the Company for the application of diseases, conditions and disorders of the central nervous system to existing and future encapsulation technology and certain additional existing technology.

In September 1997, a merger of a wholly owned subsidiary of the Company and StemCells, Inc. was completed in the form of a purchase. Through the merger, the Company acquired StemCells, Inc. for a purchase price totaling approximately $9,475,000 consisting of 1,320,691 shares of the Company's common stock and options and warrants for the purchase of 259,296 common shares at nominal consideration, valued at $7,900,000, the assumption of certain liabilities of $934,000 and transaction costs of $641,000. The purchase price was allocated, through a valuation, to license agreements valued at $1,131,000 to be amortized over three years and acquired research and development of $8,344,000 which has been expensed. As part of the acquisition of StemCells, Inc., Richard M. Rose, M.D. , became President, Chief Executive Officer and a director of CytoTherapeutics, Inc. and Dr. Irving Weissman became a director of CytoTherapeutics, Inc. Upon consummation of the merger, the Company entered into consulting arrangements with the principal scientific founders of StemCells, Inc.; Dr. Irving Weissman, Dr. Fred H. Gage and Dr. David Anderson. Additionally, in connection with the merger, the Company was granted an option by the former principal shareholders of StemCells, Inc. to repurchase approximately 500,000 of the Company's shares of Common Stock exchanged for StemCells Inc. shares, upon the occurrence of certain events as defined.

To attract and retain Drs. Rose, Weissman, Gage and Anderson, and to expedite the progress of the Company's stem cell program, the Company awarded these individuals options to acquire a total of approximately 1.6 million shares of the Company's common stock, at an exercise price of $5.25 per share, the quoted market price of the grant date; approximately 100,000 of these options are exercisable immediately, 1,031,000 of these options vest and become exercisable only on the achievement of specified milestones related to the Company's stem cell development program and the remaining 469,000 options vest over eight years. In connection with the 469,000 options issued to a non-employee, Dr. Anderson, the Company has recorded deferred compensation of $1,750,000, the fair value of such options at the date of grant, which will be amortized over an eight-year period. If the milestones specified relating to the 1,031,000 option grant are achieved, at that time the Company will record compensation expense for the excess of the quoted market price of the common stock over the exercise price of $5.25 per share for 562,000 options and the fair market value for 469,000 of such options determined using the Black-Scholes method. The Company has also designated a pool of 400,000 options to be granted to persons in a position to make a significant contribution to the success of the stem cells program.

Stem cell research will be conducted pursuant to the provisions of an agreement between the Company and Drs. Weissman and Gage providing for a two-year research plan. If the goals of the research plan are accomplished, the Company has agreed to fund continuing stems cells research. Increases in stem cells research funding of not more than 25% a year will be funded by the Company as long as the goals of the research plan are being met, provided, however, that the Company will retain the option of (i) ceasing or reducing neural stem cell research even if all research plan goals are met by accelerating the vesting of all still-achievable performance based options and (ii) ceasing or reducing non-neural stem cell research even if all plan goals are being met by affording the scientific research founders the opportunity to continue development of the non-neural stem cell research by licensing the technology related to such research to the founders in exchange for a payment to the Company equal to all funding for such research, plus royalty payments.

In 1997, the Company entered into an agreement with NeuroSpheres, Ltd. which superseded all previous license agreements and settled a dispute with NeuroSpheres, Ltd. Under the terms of the

settlement, the Company has an exclusive royalty bearing license to growth-factor responsive stem cells for transplantation and NeuroSpheres, Ltd. has an option to acquire co-exclusive rights in exchange for an up front payment of $5,000,000. NeuroSpheres, Ltd.' option expires in 1998, if unexercised. The parties have no further research obligations to each other.

In February 1997, the Company and Cognetix, Inc. entered into a collaboration and development agreement to screen selected peptides isolated by Cognetix, Inc. for possible development into therapeutic products aimed at a broad range of human disease states using the Company's cell-based delivery technology. Due to lack of certain successes under the Agreement, the Company and Cognetix, Inc. are reexamining their relationship; the Company expects this reexamination will lead to termination of the joint project under the agreement signed in February 1997. As part of the agreement with Cognetix, Inc., the Company purchased $250,000 of Cognetix, Inc. preferred stock and subject to certain milestones, is obligated to purchase as much as $1,500,000 of additional Cognetix, Inc. preferred stock. In July 1997, the Company loaned $250,000 to Cognetix, inc. which was repaid with interest in October 1997. The Company and Cognetix, Inc. have also entered into an option agreement giving the Company the right to purchase an option for up to three of Cognetix, Inc.'s compounds for use in treating eye diseases. In January 1998, the Company has exercised its option as to one protein for $100,000.

In November 1996, the Company signed collaborative development and licensing agreements with Genentech, Inc. relating to the development of products using the Company's technology to deliver certain of Genentech's proprietary growth factors to treat certain diseases of the central nervous system. Under the terms of the agreement for Parkinson's disease, Genentech, Inc. purchased 829,171 shares of Common Stock for $8,300,000 to fund development of products to treat Parkinson's disease. Additional equity purchases and other funding by Genentech, Inc. may be available for future clinical development if agreed by the parties. Upon commercialization, Genentech, Inc. and the Company will share profits from product sales in the U.S. at an agreed upon percentage and Genentech, Inc. will pay the Company a royalty for product sales outside the U.S. The Company retained manufacturing rights for all products sold.

The Company also licensed certain growth factors for the treatment of Huntington's disease and amyotrophic lateral sclerosis ("ALS"). Under the terms of the agreements, the Company is responsible for conducting and funding all preclinical and clinical development, subject to specified rights of Genentech, Inc. to participate in the development and marketing of the proposed products. Should Genentech, Inc. share in the development cost of the proposed products, the companies will share profits from certain territories at negotiated percentages. Where Genentech, Inc. does not participate in the development, upon commercialization, the Company will pay Genentech, Inc. an agreed upon royalty based on sales.

In March 1995, the Company signed a collaborative research and development agreement with Astra AB for the development and marketing of certain encapsulated-cell products to treat pain. Astra AB made an initial, non-refundable payment of $5,000,000, included in revenue from collaborative agreements in 1995, a milestone payment of $3,000,000 in 1997 and may remit up to an additional $13,000,000 subject to the achievement of certain development milestones. Under the agreement, the Company is obligated to conduct certain research and development pursuant to a four-year research plan agreed upon by the parties. Over the term of the research plan, the Company expects to receive annual research payments of $5 million to $7 million from Astra AB which should fund the majority of the research and development costs incurred by the Company under the Plan. Subject to the successful development of such products and obtaining necessary regulatory approvals, Astra AB is obligated to conduct all clinical trials of products arising from the collaboration and to seek approval for their sale. Astra AB has the exclusive worldwide right to market products covered by the agreement. Until the later of either the last to expire of all patents included in the licensed technology or a specified fixed term, the Company is entitled to a royalty on the worldwide net sales of such products in return for the marketing license granted to Astra AB and the Company's obligation to manufacture and supply products. Astra AB has the right to terminate the agreement after April 1, 1998.

Substantial additional funds will be required to support the Company's research and development programs, for acquisition of technologies and intellectual property rights, for preclinical and clinical testing of its anticipated products, pursuit of regulatory approvals, acquisition of capital equipment, expansion of laboratory and office facilities, establishment of production capabilities and for general and administrative expenses. Until the Company's operations generate significant revenues from product sales, cash reserves and proceeds from equity and debt offerings, grants and funding from collaborative arrangements will be used to fund operations.

The Company intends to pursue opportunities to obtain additional financing in the future through equity and debt financing, lease agreements related to capital equipment, grants and collaborative research arrangements. The source, timing and availability of any future financing will depend principally upon equity market conditions, interest rates and, more specifically, on the Company's continued progress in its exploratory, preclinical and clinical development programs. There can be no assurance that such funds will be available on favorable terms, if at all.

The Company expects that its existing capital resources, revenues from collaborative agreements and income earned on invested capital will be sufficient to fund its operations through 1999. The Company's cash requirements may vary, however, depending on numerous factors. Lack of necessary funds may require the Company to delay, scale back or eliminate some or all of its research and product development programs and/or its capital expenditures or to license its potential products or technologies to third parties.

The Company has conducted a review of its computer systems to identify the systems that could be affected by the "Year 2000" issue and is developing an implementation plan to resolve the issue. The Year 2000 problem is the result of computer programs being written using two digits rather than four to define the applicable year. Any of the Company's programs that have time-sensitive software may recognize a date using "00" as the year 1900 rather than the year 2000. This could result in system failures or miscalculations to existing software and converting to new software. The Year 2000 problem is not expected to pose a significant problem for the Company.

ITEM 7A. QUANTITIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT AUDITORS

Stockholders and Board of Directors
CytoTherapeutics, Inc.

We have audited the accompanying consolidated balance sheets of CytoTherapeutics, Inc. as of December 31, 1997 and 1996, and the related consolidated statements of operations, changes in redeemable stock and stockholders' equity and cash flows for each of the three years in the period ended December 31, 1997. Our audits also included the financial statement schedule listed in the Index at Item 14(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 referred to above present fairly, in all material respects, the consolidated financial position of CytoTherapeutics, Inc. at December 31, 1997 and 1996, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1997, in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ ERNST & YOUNG LLP

Boston, Massachusetts
February 6, 1998

CYTOTHERAPEUTICS, INC.

CONSOLIDATED BALANCE SHEETS

	December 31,	
	1997	1996
ASSETS		
Current assets:		
Cash and cash equivalents	$15,941,701	$19,921,584
Marketable securities	13,108,497	22,685,855
Accrued interest receivable	553,186	653,190
Other current assets	576,008	491,582
TOTAL CURRENT ASSETS	30,179,392	43,752,211
Property, plant and equipment, net	7,922,751	10,732,102
Other assets, net	6,199,323	3,912,430
TOTAL ASSETS	$44,301,466	$58,396,743
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 867,804	$1,850,925
Accrued expenses	3,241,547	2,308,844
Deferred revenue	16,144	1,859,092
Current maturities of capitalized lease obligations	419,095	553,557
Current maturities of long-term debt	658,986	695,570
TOTAL CURRENT LIABILITIES	5,203,576	7,267,988
Capitalized lease obligations, less current maturities	3,552,500	3,971,594
Long-term debt, less current maturities	555,525	4,251,008
Commitments and contingencies		
Redeemable common stock, $.01 par value; 557,754 and 815,065 shares issued and outstanding at December 31, 1997 and 1996, respectively	5,583,110	8,158,798
Common stock to be issued	506,600	--
Stockholders' equity:		
Convertible preferred stock, $.01 par value; 1,000,000 shares authorized; no shares issued and outstanding	--	--
Common stock, $.01 par value; 45,000,000 shares authorized; 17,526,220 and 15,614,333 shares issued and outstanding at December 31, 1997 and 1996, respectively	175,262	156,144
Additional paid-in capital	121,472,844	107,649,659
Accumulated deficit	(91,036,254)	(72,922,674)
Unrealized gains (losses) on marketable securities	(8,877)	14,760
Cumulative translation adjustment	--	(60,416)
Deferred compensation	(1,702,820)	(90,118)
TOTAL STOCKHOLDERS' EQUITY	28,900,155	34,747,355
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$44,301,466	$58,396,743

See accompanying notes to consolidated financial statements.

CYTOTHERAPEUTICS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

	YEAR ENDED DECEMBER 31,		
	1997	1996	1995
Revenue from collaborative agreements	$ 10,617,443	$ 7,104,284	$ 11,760,666
Operating expenses:			
Research and development	18,603,523	17,130,392	14,729,703
Acquired research and development	8,343,684	--	--
General and administrative	6,158,410	5,678,783	4,619,733
	33,105,617	22,809,175	19,349,436
LOSS FROM OPERATIONS	(22,488,174)	(15,704,891)	(7,588,770)
Other income (expense):			
Interest income	1,931,260	2,259,886	1,713,849
Interest expense	(437,991)	(618,213)	(685,470)
Gain on partial sale of Modex	3,386,808	--	--
Loss on sale/leaseback	(342,014)	--	--
Loss on equity investment	(105,931)	--	--
Other income (expense)	(57,538)	404,128	--
Currency exchange loss	--	(100,048)	--
Loss on other investment	--	--	(2,330,848)
	4,374,594	1,945,753	(1,302,469)
NET LOSS	$ (18,113,580)	$ (13,759,138)	$ (8,891,239)
NET LOSS PER SHARE	$ (1.08)	$ (.89)	$ (.69)
SHARES USED IN COMPUTING NET LOSS PER SHARE	16,704,144	15,429,564	12,799,008

See accompanying notes to consolidated financial statements.

CYTOTHERAPEUTICS, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN REDEEMABLE COMMON STOCK AND STOCKHOLDERS' EQUITY

	REDEEMABLE COMMON STOCK		COMMON STOCK		ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	UNREALIZED GAINS (LOSSES) ON MARKETABLE SECURITIES	CUMULATIVE TRANSLATION ADJUSTMENTS
	SHARES	AMOUNT	SHARES	AMOUNT				
Balances, January 1, 1995	--	$ --	11,003,568	$ 110,036	$ 73,008,958	$ (50,272,297)	$ (100,356)	$ --
Issuance of common stock	--	--	4,070,598	40,706	30,797,086		--	--
Exercise of stock options	--	--	102,831	1,028	465,614	--	--	--
Amortization of deferred compensation	--	--	--	--	--	--	--	--
Change in unrealized gains on marketable securities	--	--	--	--	--	--	231,842	--
Net loss	--	--	--	--	--	(8,891,239)	--	--
Balances, December 31, 1995	--	--	15,176,997	151,770	104,271,658	(59,163,536)	131,486	--
Issuance of common stock	--	--	168,260	1,683	1,526,118	--	--	--
Issuance of common stock under the stock purchase plan	--	--	18,338	184	140,557	--	--	--
Exercise of warrants	--	--	6,128	61	(61)	--	--	--
Issuance of common stock to consultants and employees	--	--	48,700	487	429,079	--	--	--
Common stock issued pursuant to employee benefit plan	--	--	13,719	137	162,231	--	--	--
Issuance of redeemable common stock	829,171	8,300,000	--	--	--	--	--	--
Redeemable common stock lapses	(14,106)	(141,202)	14,106	141	141,061	--	--	--
Exercise of stock options	--	--	168,085	1,681	979,016	--	--	--
Amortization of deferred compensation	--	--	--	--	--	--	--	--
Change in unrealized losses on marketable securities	--	--	--	--	--	--	(116,726)	--
Change in cumulative translation adjustment	--	--	--	--	--	--	--	(60,416)
Net loss	--	--	--	--	--	(13,759,138)	--	--
Balances, December 31, 1996	815,065	$ 8,158,798	15,614,333	$ 156,144	$ 107,649,659	$ (72,922,674)	$ 14,760	$ (60,416)

	DEFERRED COMPENSATION	TOTAL STOCKHOLDERS' EQUITY
Balances, January 1, 1995	$ (109,271)	$ 22,637,070
Issuance of common stock	--	30,837,792
Exercise of stock options	--	466,642
Amortization of deferred compensation	109,271	109,271
Change in unrealized gains on marketable securities	--	231,842
Net loss	--	(8,891,239)
Balances, December 31, 1995	--	45,391,378
Issuance of common stock	--	1,527,801
Issuance of common stock under the stock purchase plan	--	140,741
Exercise of warrants	--	--
Issuance of common stock to consultants		

and employees.....	(185,201)	244,365
Common stock issued pursuant to employee benefit plan.....	--	162,368
Issuance of redeemable common stock.....	--	--
Redeemable common stock lapses.....	--	141,202
Exercise of stock options.....	--	980,697
Amortization of deferred compensation.....	95,083	95,083
Change in unrealized losses on marketable securities.....	--	(116,726)
Change in cumulative translation adjustment.....	--	(60,416)
Net loss.....	--	(13,759,138)
Balances, December 31, 1996.....	$ (90,118)	$ 34,747,355

CYTOTHERAPEUTICS, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN REDEEMABLE COMMON STOCK AND STOCKHOLDERS' EQUITY (CONTINUED)

	REDEEMABLE COMMON STOCK		COMMON STOCK		ADDITIONAL PAID-IN	ACCUMULATED	UNREALIZED GAINS (LOSSES) ON MARKETABLE	CUMULATIVE TRANSLATION	DEFERRED	TOTAL STOCKHOLDERS' EQUITY
	SHARES	AMOUNT	SHARES	AMOUNT	CAPITAL	DEFICIT	SECURITIES	ADJUSTMENTS	COMPENSATION	
Issuance of common stock	--	--	307,548	3,074	1,552,432	--	--	--	--	1,555,506
Issuance of common stock under the stock purchase plan	--	--	31,822	319	180,103	--	--	--	--	180,422
Deferred compensation recorded in connection with the granting of stock options	--	--	--	--	1,750,000	--	--	--	(1,750,000)	--
Common stock issued pursuant to employee benefit plan	--	--	25,588	256	169,196	--	--	--	--	169,452
Issuance of common stock -- StemCells, Inc.	--	--	1,219,381	12,194	7,381,206	--	--	--	--	7,393,400
Redeemable common stock lapses	(257,311)	(2,575,688)	257,311	2,573	2,573,115	--	--	--	--	2,575,688
Exercise of stock options	--	--	75,237	752	244,427	--	--	--	--	245,179
Deferred compensation-- amortization and cancellations	--	--	(5,000)	(50)	(27,294)	--	--	--	137,298	109,954
Change in unrealized losses on marketable securities	--	--	--	--	--	--	(23,637)	--	--	(23,637)
Change in cumulative translation adjustment	--	--	--	--	--	--	--	60,416	--	
Net loss	--	--	--	--	--	(18,113,580)	--	--	--	
Balances, December 31, 1997	557,754	$5,583,110	17,526,220	$ 175,262	$121,472,844	$(91,036,254)	$ (8,877)	$ --	$(1,702,820)	

cumulative translation adjustment.....	60,416
Net loss.....	(18,113,580)
Balances, December 31, 1997.....	$28,900,155

See accompanying notes to consolidated financial statements.

CYTOTHERAPEUTICS, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	YEAR ENDED DECEMBER 31,		
	1997	1996	1995
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	$(18,113,580)	$(13,759,138)	$(8,891,239)
Adjustments to reconcile net loss to net cash used for operating activities:			
Depreciation and amortization	1,968,234	1,671,068	1,465,351
Acquired research and development	8,343,684	--	--
Amortization of deferred compensation	109,954	95,083	109,271
Common stock issued as compensation	--	406,733	--
Equity interest loss	105,931	--	--
Loss (gain) on investment	(3,386,808)	--	2,330,848
Loss on sale of fixed assets	413,856	871	--
Changes in operating assets and liabilities:			
Accrued interest receivable	100,004	140,025	(606,395)
Other current assets	(232,604)	220,688	(293,909)
Accounts payable and accrued expenses	(1,233,501)	1,077,350	183,680
Deferred revenue	(1,842,948)	109,092	1,750,000
NET CASH USED IN OPERATING ACTIVITIES	(13,767,778)	(10,038,228)	(3,952,393)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sale of Modex, net of cash disposed	2,958,199	--	--
Purchases of marketable securities	(14,182,521)	(3,083,621)	(48,127,842)
Proceeds from sales of marketable securities	23,736,242	14,924,200	24,139,057
Purchase of property, plant and equipment	(7,710,126)	(4,412,190)	(1,405,522)
Proceeds on sale of fixed assets	8,003,926	3,000	--
Purchase of other investment	(250,000)	--	(500,100)
Acquisition of other assets	(1,599,418)	(811,305)	(550,116)
StemCells assets acquired	(640,490)	--	--
Advance to Cognetix	250,000	--	--
Repayment from Cognetix	(250,000)	--	--
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	10,315,812	6,620,084	(26,444,523)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from issuance of redeemable common stock	--	8,300,000	--
Proceeds from issuance of common stock	1,905,380	1,668,542	30,837,792
Proceeds from the exercise of stock options and warrants	245,179	980,697	466,642
Proceeds from debt financings	--	4,059,947	859,832
Repayments of debt and lease obligations	(2,496,849)	(1,171,926)	(934,661)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(346,290)	13,837,260	31,229,605
Effect of exchange rate on cash and cash equivalents	(181,627)	(46,111)	--
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(3,979,883)	10,373,005	832,689
Cash and cash equivalents, January 1	19,921,584	9,548,579	8,715,890
CASH AND CASH EQUIVALENTS, DECEMBER 31	$15,941,701	$19,921,584	$9,548,579
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
INTEREST PAID	$ 436,461	$ 616,671	$ 700,806

See accompanying notes to consolidated financial statements.

CYTOTHERAPEUTICS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1997

1. NATURE OF BUSINESS

CytoTherapeutics, Inc. (the "Company") is a biopharmaceutical company engaged in the development of cell-based therapeutics designed to deliver therapeutic substances to the central nervous system or regenerate damaged tissue.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

The 1997 consolidated financial statements include accounts of the Company and StemCells, Inc., a wholly owned subsidiary. The 1996 consolidated financial statements include accounts of the Company and Modex Therapeutiques SA, a 50%-owned subsidiary. Significant intercompany accounts have been eliminated in consolidation.

USE OF ESTIMATES

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles 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.

CASH, CASH EQUIVALENTS AND MARKETABLE SECURITIES

Cash and cash equivalents include funds held in investments with original maturities of three months or less. The Company's policy regarding selection of investments, pending their use, is to insure safety, liquidity, and capital preservation while obtaining a reasonable rate of return. Marketable securities consist of investments in agencies of the U.S. government, investment-grade corporate notes and money market funds. The fair values for marketable securities are based on quoted market prices.

The Company determines the appropriate classification of cash equivalents and marketable securities at the time of purchase and reevaluates such designation as of each balance sheet date. The Company has classified such holdings as available-for-sale securities, which are carried at fair value, with unrealized gains and losses reported as a separate component of stockholders' equity.

PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, including that held under capitalized lease obligations, is stated at cost and depreciated using the straight-line method over the estimated life of the respective asset, as follows:

Building and improvements	3 - 15 years
Machinery and equipment	3 - 10 years
Furniture and fixtures	3 - 10 years

PATENT COSTS

The Company capitalizes certain patent costs related to patent applications. Accumulated costs are amortized over the estimated economic life of the patents, not to exceed 17 years, using the straight-line method, commencing at the time the patent is issued. Costs related to patent applications are written off to

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

expense at the time such patents are deemed to have no continuing value. At December 31, 1997 and 1996, total costs capitalized were $3,486,000 and $2,887,000 and the related accumulated amortization was $208,000 and $126,000, respectively. Patent expense totaled $365,000, $249,000, and $195,000 in 1997, 1996 and 1995, respectively.

STOCK BASED COMPENSATION

The Company grants qualified stock options for a fixed number of shares to employees with an exercise price equal to the fair market value of the shares at the date of grant. The Company accounts for stock option grants in accordance with APB Opinion No. 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES, and, accordingly, recognizes no compensation expense for qualified stock option grants.

For certain non-qualified stock options granted, the Company recognizes as compensation expense the excess of the deemed fair value of the common stock issuable upon exercise of such options over the aggregate exercise price of such options. The compensation is amortized over the vesting period of each option or the recipient's term of employment, if shorter.

INCOME TAXES

The liability method is used to account for income taxes. Deferred tax assets and liabilities are determined based on differences between financial reporting and income tax bases of assets and liabilities as well as net operating loss carryforwards and are measured using the enacted tax rates and laws that are expected to be in effect when the differences reverse. Deferred tax assets may be reduced by a valuation allowance to reflect the uncertainty associated with their ultimate realization.

REVENUE FROM COLLABORATIVE AGREEMENTS

Revenues from collaborative agreements are recognized as earned upon either the incurrence of reimbursable expenses or the achievement of certain milestones. Payments received in advance of research performed are designated as deferred revenue.

FOREIGN CURRENCY TRANSLATION

Prior to the sale of a majority ownership position in Modex, assets and liabilities of operations outside the United States are translated into United States dollars using current exchange rates; revenue and expense items are translated into United Stated dollars using a weighted average exchange rate for the period. The gains and losses resulting from such translation are accumulated as a separate component of shareholders' equity, whereas gains and losses resulting from foreign currency transactions generally are included in results of operations.

NET LOSS PER SHARE

Net loss per share is computed using the weighted average number of shares of common stock outstanding. Common equivalent shares from stock options and warrants are excluded, as their effect is antidilutive.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

In 1997, the Company adopted Statement of Accounting Standards No. 128, EARNINGS PER SHARE (EPS) which is effective for both interim and annual financial statements for periods ended after December 15, 1997. Under Statement 128, primary EPS computed in accordance with Opinion 15 has been replaced with a simpler calculation called basic EPS. Basic EPS is calculated by dividing income available to common stockholders by the weighted average common shares outstanding. Fully dilutive EPS did not change significantly, but has been renamed diluted EPS. The adoption of Statement 128 had no effect on the Company's financial statements since common equivalent shares from stock options and warrants have been excluded as their effect is antidilutive.

IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In June 1997, the FASB issued Statement No. 130, "REPORTING COMPREHENSIVE INCOME," and Statement No. 131, "DISCLOSURES ABOUT SEGMENTS OF AN ENTERPRISE AND RELATED INFORMATION." Statement No. 130 establishes standards for reporting and display of comprehensive income and its components. Statement No. 131 establishes standards for the way that public companies report information about operating segments in financial statements. This Statement supersedes Statement No. 14, "FINANCIAL REPORTING FOR SEGMENTS OF A BUSINESS ENTERPRISE," but retains the requirements to report information about major customers. Statements 130 and 131 are effective for the Company in fiscal 1998. The Company does not believe that the adoption of these Statements will have a material effect on the Company's financial statements.

3. STEMCELLS, INC.

In September 1997, a merger of a wholly owned subsidiary of the Company and StemCells, Inc. was completed in the form of a purchase. Through the merger, the Company acquired StemCells for a purchase price totaling approximately $9,475,000, consisting of 1,320,691 shares of the Company's common stock and options and warrants for the purchase of 259,296 common shares at nominal consideration, valued at $7,900,000 in the aggregate, the assumption of certain liabilities of $934,000 and transaction costs of $641,000. The purchase price was allocated, through a valuation, to license agreements valued at $1,131,000 to be amortized over three years and acquired research and development of $8,344,000 which has been expensed. As part of the acquisition of StemCells, Richard M. Rose, M.D., became President, Chief Executive Officer and director of the Company and Dr. Irving Weissman became a director of the Company.

Upon consummation of the merger, the Company entered into consulting arrangements with the principal scientific founders of StemCells: Dr. Irving Weissman, Dr. Fred H. Gage and Dr. David Anderson. Additionally, in connection with the merger, the Company was granted an option by the former principal shareholders of StemCells to repurchase approximately 500,000 of the Company's shares of Common Stock exchanged for StemCells shares, upon the occurrence of certain events as defined.

To attract and retain Drs. Rose, Weissman, Gage and Anderson, and to expedite the progress of the Company's stem cell program, the Company awarded these individuals options to acquire a total of approximately 1.6 million shares of the Company's common stock, at an exercise price of $5.25 per share, the quoted market price at the grant date; approximately 100,000 of these options are exercisable immediately, 1,031,000 of these options vest and become exercisable only upon the achievement of specified milestones related to the Company's stem cell development program and the remaining 469,000

3. STEMCELLS, INC. (CONTINUED)
options vest over eight years. In connection with the 469,000 options issued to a non-employee, Dr. Anderson, the Company has recorded deferred compensation of $1,750,000, the fair value of such options at the date of grant, which will be amortized over an eight-year period. If the milestones specified relating to the 1,031,000 option grant are achieved, at that time the Company will record compensation expense for the excess of the quoted market price of the common stock over the exercise price of $5.25 per share for 562,000 options and the fair market value for 469,000 of such options determined using the Black-Scholes method. The Company has also designated a pool of 400,000 options to be granted to persons in a position to make a significant contribution to the success of the stem cell program.

Stem cell research will be conducted pursuant to the provisions of an agreement between the Company and Drs. Weissman and Gage providing for a two-year research plan. If the goals of the research plan are accomplished, the Company has agreed to fund continuing stem cell research. Increases in stem cells research funding of not more than 25% a year will be funded by the Company as long as the goals of the research plan are being met. However, the Company will retain the option of (i) ceasing or reducing neural stem cell research even if all research plan goals are met, but will be required to accelerate the vesting of all still-achievable performance based stock options, and (ii) ceasing or reducing non-neural stem cell research even if all plan goals are being met by affording the scientific research founders the opportunity to continue development of the non-neural stem cell research by licensing the technology related to such research to the founders in exchange for a payment to the Company equal to all prior Company funding for such research, plus royalty payments.

4. MODEX

In October 1997, the Company completed a series of transactions which resulted in the establishment of its previously 50%-owned Swiss subsidiary, Modex Therapeutiques SA ("Modex") as an independent company. In the transactions, the Company reduced its ownership interest from 50% to approximately 25% in exchange for $4 million cash and elimination of its prior contingent obligation to contribute an additional Sfr 2.4 million (approximately $1.7 million) to Modex in July 1998. In the transactions, all of the put and call arrangements between the Company and other stockholders of Modex were eliminated and the Company forgave $463,000 due from Modex to the Company. The Company recorded a gain on the transactions of $3,387,000 and will account for its now approximately 25% investment under the equity method.

The Company and Modex also modified the terms of their existing royalty-bearing Cross License Agreement to (i) expand the field in which Modex is exclusively licensed to apply the Company's proprietary encapsulated cell technology to include, in addition to the original field of diabetes, obesity and anemia, the treatment of hemophilia A and B utilizing Factor VIII and/or Factor IX and two additional applications to be agreed to by the Company and Modex; (ii) eliminate the requirement to make future milestone payments to Modex of up to 300,000 shares of the Company's common stock; (iii) limit the scope of the Company's technology licensed to Modex to existing and future encapsulation technology; and (iv) specify the terms under which the Company will manufacture any products Modex may develop based on the Company's technology and grant Modex an option to manufacture or have manufactured such products on payment of a higher royalty. The Cross License Agreement continues to provide for the payment of royalties from Modex to the Company on the sale of any licensed products. The revised agreement similarly limits the scope of the Modex technology exclusively licensed, on a royalty-bearing

4. MODEX (CONTINUED)
basis, to the Company for the application of diseases, conditions and disorders of the central nervous system to existing and future encapsulation technology and certain additional existing technology.

5. MARKETABLE SECURITIES

The following is a summary of available-for-sale securities:

	DECEMBER 31, 1997			
	COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. government securities	$3,153,834	$ 92	$ (3,951)	$3,149,975
U.S. corporate securities	21,261,850	1,645	(6,663)	21,256,832
Total debt securities	$24,415,684	$ 1,737	$ (10,614)	24,406,807
Debt securities included in cash and cash equivalents				(11,298,310)
Debt securities included in marketable securities				$13,108,497

	DECEMBER 31, 1996			
	COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. government securities	$2,007,823	$ --	$ (14,023)	$1,993,800
U.S. corporate securities	21,651,507	28,784	--	21,680,291
Total debt securities	$23,659,330	$ 28,784	$ (14,023)	23,674,091
Debt securities included in cash and cash equivalents				(988,236)
Debt securities included in marketable securities				$22,685,855

Maturities of marketable securities held at December 31, 1997, are as follows:

Less than one year	$22,397,607
One through five years	2,009,200
	$24,406,807

6. OTHER INVESTMENT

In December 1993, the Company sold substantially all of the assets of its primary cell diabetes product development program, including related equipment, and licensed related intellectual property to Neocrin Company in exchange for preferred stock representing a then 10% ownership interest with a fair market value of $2,030,748. The transaction resulted in a gain before closing expenses of $1,957,913 and a net gain of $1,780,209. In February 1995, the Company purchased an additional $500,100 of Neocrin's preferred stock at the current market value, as required under the original purchase agreement.

In December 1995, Neocrin completed an equity offering, in which the Company did not participate, at a valuation substantially lower than prior financings. As a result, the Company determined that the carrying value in its investment had been permanently impaired and provided a $2,330,848 valuation reserve to reduce the investment value to $200,000.

7. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following:

	DECEMBER 31,	
	1997	1996
Land	$ --	$ 278,774
Building and improvements	4,977,906	6,207,679
Machinery and equipment	8,549,405	7,554,825
Furniture and fixtures	717,377	1,424,907
Construction in progress	23,947	2,214,318
	14,268,635	17,680,503
Less accumulated depreciation and amortization	6,345,884	6,948,401
	$ 7,922,751	$ 10,732,102

Depreciation and amortization expense was $1,778,000, $1,564,000, and $1,431,000 for the years ending December 31, 1997, 1996 and 1995, respectively.

Certain property, plant and equipment have been acquired under capitalized lease obligations. These assets totaled $6,587,000 and $8,910,000, at December 31, 1997 and 1996, respectively, with related accumulated amortization of $2,297,000 and $3,947,000 at December 31, 1997 and 1996, respectively.

In connection with the Company's new facility, the Company capitalized $210,000 and $42,000 of interest costs in 1997 and 1996, respectively.

8. OTHER ASSETS

Other assets are as follows:

	DECEMBER 31,	
	1997	1996
Patents, net	$ 3,278,709	$ 2,760,593
License agreements, net	1,036,750	--
Security deposit--building lease	750,000	--
Restricted cash	552,357	497,956
Other investments	450,000	200,000
Deferred financing costs, net	131,507	297,698
Organizational costs, net	--	156,183
	$ 6,199,323	$ 3,912,430

At December 31, 1997 and 1996, accumulated amortization was $302,000 and $126,000, respectively, for patents and license agreements.

9. ACCRUED EXPENSES

Accrued expenses are as follows:

	DECEMBER 31,	
	1997	1996
External services	$ 1,709,818	$ 537,605
Employee compensation	755,951	824,910
Collaborative research	499,575	413,497
Other	276,203	532,832
	$ 3,241,547	$ 2,308,844

10. LEASES

The Company has undertaken direct financing transactions with the State of Rhode Island and received proceeds from the issuance of industrial revenue bonds totaling $5,000,000 to finance the construction of its pilot manufacturing facility. The related leases are structured such that lease payments will fully fund all semiannual interest payments and annual principal payments through maturity in August 2014. Fixed interest rates vary with the respective bonds' maturities, ranging from 5.1% to 9.5%. The bonds contain certain restrictive covenants which limit, among other things, the payment of cash dividends and the sale of assets. In addition, the Company is required to maintain a debt service reserve, which totals $532,000, until December 1999.

In 1997, the Company completed construction of a new headquarters and laboratory facility. In November 1997, the Company entered into sale and leaseback agreement with a real estate investment trust. Under the terms of these agreements, the Company sold its new facility for $8,000,000 incurring a $342,000 loss on the sale. The Company simultaneously entered into a fifteen-year lease for the facility. The lease agreement calls for minimum rent of $750,000 for the first five years, $937,500 for years six to

10. LEASES (CONTINUED)
ten, $1,171,900 for years eleven to fourteen and $1,465,000 in year fifteen with a $750,000 security deposit held for the term of the lease.

Future minimum capitalized lease obligations with noncancelable terms in excess of one year at December 31, 1997, are as follows:

1998	$ 753,788
1999	624,030
2000	607,518
2001	589,634
2002	510,553
Thereafter	3,568,452
Total minimum lease payments	6,653,975
Less amounts representing interest	2,682,380
Present value of minimum lease payments	3,971,595
Less current maturities	419,095
Capitalized lease obligations, less current maturities	$3,552,500

Rent expense for the years ended December 31, 1997, 1996 and 1995, was $499,000, $495,000, and $463,000, respectively.

11. LONG-TERM DEBT

Long-term debt is as follows:

	DECEMBER 31, 1997	DECEMBER 31, 1996
Term note payable, interest at the prime rate plus 1/2% (9% at December 31, 1997), principal payments commence in August 1998, due ratably through May 2000; secured by certain equipment	$ 740,700	$ 740,700
Term note payable, interest at the prime rate plus 1/2% (9% at December 31, 1997), due ratably through December 1998; secured by certain equipment	432,588	867,227
Convertible subordinated note (Sfr 2,400,000)	--	1,788,775
Facilities term note payable	--	1,450,000
Other	41,223	99,876
	1,214,511	4,946,578
Current maturities of long-term debt	658,986	695,570
Long-term debt, less current maturities	$ 555,525	$ 4,251,008

Both term note agreements include certain restrictive covenants that limit, among other things, the payment of dividends, sale of assets and the incurrence of additional indebtedness. As noted above, in

11. LONG-TERM DEBT (CONTINUED)
1997, the Company ceased to consolidate the accounts of Modex Therapeutiques SA, which included the convertible subordinated note. In conjunction with the sale and leaseback of the Company's headquarters facility in 1997, the facilities term note was repaid.

Maturities of long-term debt for the years ending December 31 are as follows:

1998	$ 658,986
1999	370,350
2000	185,175
	$1,214,511

12. REDEEMABLE COMMON STOCK

Under a research agreement to fund development of products to treat Parkinson's disease (see Note 15), Genentech, Inc. purchased 829,171 shares of common stock for $8.3 million in December 1996. If the agreement is terminated and the funds received from the sale of common stock exceed by more than $1 million the expenses incurred by the Company in connection with such development, Genentech, Inc. has the right to require the Company to repurchase shares of its Common Stock having a value equal to the amount of overfunding, at the share price paid by Genentech. Accordingly, the common stock is classified as redeemable common stock until such time as the related funds are expended. At December 31, 1997, $2,717,000 had been spent on the collaboration with Genentech and, accordingly, the Company has reclassified those common shares and related value to stockholders' equity.

13. COMMON STOCK TO BE ISSUED

The merger with StemCells, Inc. required that StemCells shareholders tender their StemCells shares and receive shares of CytoTherapeutics in exchange. At December 31, 1997, 27,087 shares of StemCells common stock and promissory notes totaling $168,750 remained to be tendered in exchange for 101,310 shares of CytoTherapeutics' Common Stock with a value of $506,600 at the date of merger.

14. STOCKHOLDERS' EQUITY

STOCK OPTION AND EMPLOYEE STOCK PURCHASE PLANS

The Company has adopted several stock plans which provide for the issuance of incentive and nonqualified stock options, performance awards and stock appreciation rights, at prices to be determined by the Board of Directors, as well as the purchase of Common Stock under an employee stock purchase plan at a discount to the market price. In the case of incentive stock options, such price will not be less than the fair market value on the date of grant or within 3 months of termination. Options generally vest ratably over four years and are exercisable for ten years from the date of grant or within three months of termination. At December 31, 1997, the Company had reserved 3,116,312 shares of common stock for the exercise of stock options.

14. STOCKHOLDERS' EQUITY (CONTINUED)

The following table presents the combined activity of the Company's stock option plans (exclusive of the plans noted below) for the years ended December 31:

	1997		1996		1995	
	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE	OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
Outstanding at January 1.....	2,423,025	$ 8.34	1,921,284	$ 7.72	1,480,844	$ 7.21
Granted.....	679,074	5.33	852,160	9.48	678,604	8.35
Exercised.....	(82,737)	2.96	(168,085)	5.83	(102,831)	4.54
Canceled.....	(572,789)	9.21	(182,334)	9.42	(135,333)	7.77
Outstanding at December 31.....	2,446,573	$ 7.48	2,423,025	$ 8.34	1,921,284	$ 7.72
Options exercisable at December 31.....	1,338,163	$ 7.79	1,105,251	$ 7.11	839,260	$ 6.33

In addition to the options noted above, in conjunction with the StemCells merger, StemCell's options were exchanged for options to purchase 250,344 shares of the Company's common stock at $.01 per share originally issued under a prior StemCells option plan; 75,384 of these options are exercisable at December 31, 1997, 96,750 of these options vest and become exercisable only upon achievement of specified milestones, and the remaining 78,210 options vest over three years from the date of grant. Additionally, the Company adopted the 1997 CytoTherapeutics, Inc. StemCells Research Stock Option Plan (the StemCells Research Plan) whereby an additional 2,000,000 shares of common stock has been reserved. During 1997, the Company awarded options under the StemCells Research Plan to purchase 1.6 million shares of the Company's Common Stock to the Chief Executive Officer and scientific founders of StemCells at an exercise price of $5.25 per share; approximately 100,000 of these options are exercisable immediately, 1,031,000 of these options vest and become exercisable only upon achievement of specified milestones and the remaining 469,000 options vest over eight years.

FAS 123 DISCLOSURES

The Company has adopted the disclosure provisions only of Statement of Financial Accounting Standards No. 123, ACCOUNTING FOR STOCK-BASED COMPENSATION ("FAS 123") and will continue to account for its stock option plans in accordance with the provisions of APB 25, ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES.

14. STOCKHOLDERS' EQUITY (CONTINUED)

The following table presents weighted average price and life information about significant option groups outstanding at December 31, 1997:

	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
RANGE OF EXERCISE PRICES	NUMBER OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE (YRS.)	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER EXERCISABLE	WEIGHTED AVERAGE EXERCISE PRICE
Less than $5.00	286,189	4.85	$ 1.85	256,216	$ 1.73
$5.01 - $10.00	1,593,654	8.13	6.89	662,756	7.59
Greater than $10.00	566,730	6.74	12.01	419,191	11.81
	2,446,573			1,338,163	

Pursuant to the requirements of FAS 123, the following are the pro forma net loss and net loss per share for 1997, 1996, and 1995, as if the compensation cost for the option plans and the stock purchase plan had been determined based on the fair value at the grant date for grants in 1997, 1996, and 1995, consistent with the provisions of FAS 123:

	1997		1996		1995	
	AS REPORTED	PRO FORMA	AS REPORTED	PRO FORMA	AS REPORTED	PRO FORMA
Net loss	$ (18,113,580)	$ (19,924,437)	$ (13,759,138)	$ (14,931,000)	$ (8,891,239)	$ (9,161,000)
Net loss per share	$ (1.08)	$ (1.19)	$ (.89)	$ (.97)	$ (.69)	$ (.72)

The weighted average fair value per share of options granted during 1997, 1996 and 1995, was $3.40, $5.67, and $4.84, respectively. The fair value of options and shares issued pursuant to the stock purchase plan at the date of grant were estimated using the Black-Scholes model with the following weighted average assumptions:

	OPTIONS			STOCK PURCHASE PLAN		
	1997	1996	1995	1997	1996	1995
Expected life (years)	5	5	5	.5	5	.5
Interest rate	6.2%	6.5%	5.8%	5.5%	6.5%	5.1%
Volatility	59.0%	63.0%	62.0%	59.0%	63.0%	62.0%

The Company has never declared nor paid dividends on any of its capital stock and does not expect to do so in the foreseeable future.

The effects on 1997, 1996 and 1995 pro forma net loss and net loss per share of expensing the estimated fair value of stock options and shares issued pursuant to the stock purchase plan are not necessarily representative of the effects on reporting the results of operations for future years as the period presented includes only one, two and three years, respectively, of option grants under the Company's plans. As required by FAS 123, the Company has used the Black-Scholes model for option valuation, which method may not accurately value the options described.

14. STOCKHOLDERS' EQUITY (CONTINUED)
STOCK WARRANTS

In conjunction with StemCells merger, the Company has exchanged StemCells warrants for warrants to purchase 8,952 shares of Company common stock at $4.71 per share. In conjunction with various equipment leasing agreements, the Company has outstanding warrants to purchase 31,545 shares of common stock at prices ranging from $4.00 to $9.00 per share. The warrants expire through October 2000.

In connection with a public offering of common stock in April 1995, the Company issued warrants to purchase 434,500 shares of common stock at $8 per share. The warrants are nontransferable and expire in April 2000, subject to certain required exercise provisions. In addition to the foregoing rights, the holder of such warrants has the right, in the event the Company issues additional shares of common stock or other securities convertible into common stock, to purchase at the then market price of such common stock, sufficient additional shares of common stock to maintain the warrant holder's percentage ownership of the Company's Common Stock at 15%. This right, subject to certain conditions and limitations, expires in April 2000.

COMMON STOCK RESERVED

The Company has reserved 7,374,000 shares of common stock for the exercise of options, warrants and other contingent issuances of common stock.

15. RESEARCH AGREEMENTS

In November 1997, StemCells, Inc., a wholly-owned subsidiary of the Company, signed a Research Funding and Option Agreement with The Scripps Research Institute ("Scripps") relating to stem-cell research. Under the terms of the Agreement, StemCells agreed to fund $931,000 of research at Scripps over a period of three years. StemCells has paid $77,000 at December 31, 1997. In addition, the Company agreed to issue to Scripps 4,837 shares of the Company's common stock and a stock option to purchase 9,674 shares of the Company's Common Stock with an exercise price of $.01 per share upon the achievement of specified milestones. Under the Agreement, StemCells has an option for an exclusive license to the inventions resulting from the sponsored research, subject to the payment of royalties and certain other amounts, and is obligated to make payments totaling $425,000 for achievement of certain milestones.

In February 1997, the Company and Cognetix, Inc. entered into a Collaboration and Development Agreement to screen selected peptides isolated by Cognetix for possible development into therapeutic products aimed at a broad range of human disease states using CytoTherapeutic's cell-based delivery technology. Continuation of the Agreement is contingent upon meeting an agreed-upon proof of concept test. The companies will generally share expenses associated with the development of any specific product candidate and any resulting revenues, except as otherwise determined on a product-by-product basis. As part of the agreement with Cognetix, the Company has purchased $250,000 of Cognetix preferred stock and, subject to certain milestones, is obligated to purchase as much as $1,500,000 of additional Cognetix stock over the next year. In July 1997, the Company loaned $250,000 to Cognetix which was repaid with interest in October 1997.

In 1997, the Company entered into an agreement with Neurospheres, Ltd. which superseded all previous licensing agreements and settled a dispute with Neurospheres. Under the terms of the settlement,

15. RESEARCH AGREEMENTS (CONTINUED)
the Company has an exclusive royalty bearing license for growth-factor responsive stem cells for transplantation and Neurospheres has an option to acquire co-exclusive rights in exchange for an upfront payment of $5,000,000. Neurospheres' option expires in 1998, if unexercised. The parties have no further research obligations to each other.

In November 1996, the Company signed collaborative development and licensing agreements with Genentech, Inc. relating to the development of products using the Company's technology to deliver certain of Genentech's proprietary growth factors to treat certain diseases of the central nervous system. Under the terms of the agreement, Genentech purchased 829,171 shares of redeemable common stock for $8.3 million to fund development of products to treat Parkinson's disease. Additional equity purchases and other funding by Genentech may be available for future clinical development if agreed by the parties. Upon commercialization, Genentech and the Company will share profits from product sales in the United States at an agreed upon percentage and Genentech will pay the Company a royalty for product sales outside the U.S. The Company retained manufacturing rights for all products sold.

The Company also licensed growth factors for the treatment of Huntington's disease and for amyotrophic lateral sclerosis ("ALS"). Under the terms of the agreements, the Company is responsible for conducting and funding all preclinical and clinical development, subject to specified rights of Genentech to participate in the development and marketing of the proposed products. Should Genentech share in the development costs of the proposed products, the companies will share profits from certain territories at negotiated percentages. Where Genentech does not participate in the development, upon commercialization, the Company will pay Genentech an agreed upon royalty based on sales.

In March 1995, the Company signed a collaborative research and development agreement with Astra AB for the development and marketing of encapsulated-cell products to treat pain. Astra made an initial, nonrefundable payment of $5,000,000, included in revenue from collaborative agreements in 1995, a milestone payment of $3,000,000 in 1997 and may remit up to an additional $13,000,000 subject to the achievement of certain development milestones. Under the agreement, the Company is obligated to conduct certain research and development pursuant to a four-year research plan agreed upon by the parties. Over the term of the research plan, the Company expects to receive annual payments of $5 million to $7 million from Astra which should approximate the research and development costs incurred by the Company under the Plan. Subject to successful product development and obtaining necessary regulatory approvals, Astra is obligated to conduct all clinical trials of products arising from the collaboration and to seek approval for their sale. Astra has the exclusive worldwide right to market products covered by the agreement. Until the later of either expiration of all patents included in the licensed technology or a specified term, the Company is entitled to a royalty on the worldwide net sales of such products in return for the marketing license granted to Astra and the Company's obligation to manufacture and supply products. Astra has the right to terminate the agreement after April 1, 1998.

The Company has entered into other collaborative research agreements whereby the Company funds specific research programs. Pursuant to such agreements, the Company is typically granted rights to the related intellectual property or an option to obtain such rights on terms to be agreed, in exchange for research funding and specified royalties on any resulting product revenue. To date, the Company's principal academic collaborations have been with Brown University and Dr. Aebischer and Centre Hospitalier Universitaire Vaudois in Switzerland. Research and development expenses incurred under

15. RESEARCH AGREEMENTS (CONTINUED)
these collaborations amounted to approximately $1,326,000, $1,337,000, and $1,008,000 for the years ended December 31, 1997, 1996 and 1995, respectively.

16. INCOME TAXES

Due to net losses incurred by the Company in each year since inception, no provision for income taxes has been recorded. At December 31, 1997, the Company had tax net operating loss carryforwards of $24,943,000 and research and development tax credit carryforwards of $2,963,000 which expire at various times through 2012. Due to the "change in ownership" provisions of the Tax Reform Act of 1986, the Company's utilization of its net operating loss carryforwards and tax credits may be subject to annual limitation in future periods.

Significant components of the Company's deferred tax assets and liabilities are as follows:

	DECEMBER 31,	
	1997	1996
Deferred tax assets:		
Capitalized research and development costs	$ 23,876,000	$ 21,286,000
Net operating losses	9,977,000	8,648,000
Research and development credits	2,963,000	2,251,000
Other	275,000	316,000
	37,091,000	32,501,000
Deferred tax liabilities:		
Patents	1,296,000	1,096,000
	35,795,000	31,405,000
Valuation allowance	(35,795,000)	(31,405,000)
Net deferred tax assets	$ --	$ --

Since there is uncertainty relating to the ultimate use of the loss carryforwards and tax credits, a valuation allowance has been recognized at December 31, 1997 and 1996, to fully offset the Company's deferred tax assets. The valuation allowance increased $4,390,000 in 1997, due primarily to the increases in capitalized research and development costs, net operating loss carryforwards and tax credits.

17. EMPLOYEE RETIREMENT PLAN

The Company has a qualified defined contribution plan covering substantially all employees. Participants are allowed to contribute a fixed percentage of their annual compensation to the plan and the Company may match a percentage of that contribution. The Company matches 50% of employee contributions, up to 6% of employee compensation, with the Company's common stock. The related expense was $169,000, $162,000, and $131,000 for the years ended December 31, 1997, 1996 and 1995, respectively.

18. CONTINGENCIES

The Company is routinely involved in arbitration, litigation and other matters as part of the ordinary course of its business. While the resolution of any matter may have an impact on the Company's financial results for a particular reporting period, management believes the ultimate disposition of these matters will not have a materially adverse effect on the Company's consolidated financial position or results of operations.

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

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT, PROMOTERS AND CONTROL PERSONS

DIRECTORS AND EXECUTIVE OFFICERS

The sections entitled "Election of Directors" and "Executive Officer" in the Company's definitive proxy statement for its 1998 Annual Meeting of Shareholders are hereby incorporated by reference.

ITEM 11. EXECUTIVE COMPENSATION

The section entitled "Executive Compensation" in the Company's definitive proxy statement for its 1998 Annual Meeting of Shareholders is hereby incorporated by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The section entitled "Share Ownership" in the Company's definitive proxy statement for its 1998 Annual Meeting of Shareholders is hereby incorporated by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The section entitled "Certain Relationships and Related Transactions" in the Company's definitive proxy statement for its 1998 Annual Meeting of Shareholders is hereby incorporated by reference.

PART IV

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

(a) DOCUMENTS FILED AS PART OF THIS FORM 10-K.

(1) Financial Statement Schedules:

Schedules not included herein are omitted because they are not applicable or the required information appears in the Financial Statements or Notes thereto.

(2) Exhibits.

EXHIBIT NO.	TITLE OR DESCRIPTION
3.1*	Restated Certificate of Incorporation of the Registrant.
3.2++	Amended and Restated By-Laws of the Registrant.
4.1*	Specimen Common Stock Certificate.
4.2++++	Form of Warrant Certificate issued to a certain purchaser of the Registrant's Common Stock in April 1995.
10.4*	Amendment to Registration Rights dated as of February 14, 1992 among the Registrant and certain of its stockholders.
10.5* **	Research Agreement dated March 1, 1989 between the Registrant and Brown University as amended by Modification No. 1 dated December 21, 1990, Modification No. 2 dated February 22, 1991 and Modification No. 3 dated November 1, 1991.

EXHIBIT NO.	TITLE OR DESCRIPTION
10.5A*	Letter Agreement dated March 4, 1992 between the Registrant and Brown University.
10.6*	License Agreement dated March 16, 1989 between the Registrant and Brown University, as amended by Amendment Agreement dated May 2, 1991.
10.7*	Research Agreement dated March 16, 1989 between Registrant and Washington University.
10.12*	Employment Agreement dated January 3, 1991 between the Registrant and Dr. Seth A. Rudnick.
10.15*	Form of at-will Employment Agreement between the Registrant and most of its employees.
10.16*	Agreement for Consulting Services dated March 16, 1989 between the Registrant and Dr. Patrick Aebischer.
10.18*	Agreement for Consulting Services dated March 16, 1989 between the Registrant and Dr. Paul Lacy.
10.20*	Form of Agreement for Consulting Services between the Registrant and members of its Scientific Advisory Board.
10.21*	Form of Nondisclosure Agreement between the Registrant and its Contractors.
10.22*	Funding Agreement dated June 22, 1989 between the Registrant and the Rhode Island Partnership for Science and Technology.
10.28*	Master Lease and Warrant Agreement dated April 23, 1991 between the Registrant and PacifiCorp Credit, Inc.
10.29*	1988 Stock Option Plan.
10.30*	1992 Equity Incentive Plan.
10.31*	1992 Stock Option Plan for Non-Employee Directors.
10.32*	1992 Employee Stock Purchase Plan.
10.35#	Consulting Agreement dated as of September 1, 1992 between Dr. Edwin C. Cadman and the Registrant.
10.36**#	Letter Agreement between Registrant and Dr. Patrick Aebischer dated October 13, 1992 as amended by a letter agreement dated December 23, 1993.
10.37+	Employment Agreement dated September 9, 1992 between Registrant and Frederic A. Eustis, III.
10.41**!!!!	Development and Supply Agreement dated December 1993, between Registrant and AKZO Faser AG.
10.42**!!!!	Asset Transfer Agreement dated as of December 23, 1994, between Registrant and Neocrin Company.
10.43##**	Research Agreement dated as of February 1, 1994 between Genentech, Inc. and Registrant.
10.44##**	Research Agreement dated as of March 16, 1994 between NeuroSpheres, Ltd. and Registrant.

EXHIBIT NO.	TITLE OR DESCRIPTION
10.46++	Termination Agreement dated as of August 4, 1994 between Registrant and Medtronic, Inc.
10.47++	Term Loan Agreement dated as of September 30, 1994 between The First National Bank of Boston and Registrant.
10.48++	Lease Agreement between the Registrant and Rhode Island Industrial Facilities Corporation, dated as of August 1, 1992.
10.49++	First Amendment to Lease Agreement between Registrant and The Rhode Island Industrial Facilities Corporation dated as of September 15, 1994.
10.50++	Supplementary Agreement dated as of July 1, 1994 between Akzo Nobel Faser AG and the Registrant.
10.51**++++	Development, Marketing and License Agreement, dated as of March 30, 1995, between Registrant and Astra AB.
10.52++++	Form of Unit Purchase Agreement to be executed by the purchasers of the Common Stock and Warrants offered in April 1995.
10.53+++	Form of Common Stock Purchase Agreement to be executed among the Registrant and certain purchasers of the Registrant's Common Stock.
10.54!**	Research and Commercialization Agreement dated as of September 4, 1995 among the Company, Dr. Patrick Aebischer and Canton of Vaud, Switzerland.
10.55!!	Employment agreement dated as of July 2, 1996 between Dr. Sandra Nusinoff Lehrman and Registrant.
10.56!!	Consulting agreement dated as of September 1, 1996 between Dr. Edwin C. Cadman and the Registrant.
10.57!!	Convertible loan agreement dated as of July 10, 1996 between the Company and Modex Therapeutiques SA.
10.58	Lease Agreement dated as of November 21, 1997 by and between Hub RI Properties Trust, as Landlord, and CytoTherapeutics, Inc., as Tenant.
10.59!!	Modex Therapeutiques SA stockholders voting agreement dated as of July 10, 1996 among Modex, the Company, the Societe Financiere Valoria SA and the other stockholders listed therein.
10.60!!	CTI individual stockholders option agreement dated as of July 10, 1996 among the Company and the individuals listed therein.
10.61!!	CTI--Valoria option agreement dated of July 10, 1996 between the Company and the Societe Financiere Valoria SA.
10.62**!!!	Development Collaboration and License Agreement dated as of November 22, 1996 between Genentech, Inc. and the Registrant.
10.63!!!	Consulting Agreement dated as of December 1, 1996, between Peter Simon and the Registrant.
10.64!!!	Term Loan Agreement dated as of October 22, 1996 between The First National Bank of Boston and the Registrant.

EXHIBIT NO.	TITLE OR DESCRIPTION
10.65***	Agreement and Plan of Merger dated as of August 13, 1997 among StemCells, Inc., the Registrant and CTI Acquisition Corp.
10.67***	Consulting Agreement dated as of September 25, 1997 between Dr. Irving Weissman and the Registrant.
10.68	Letter Agreement between each of Dr. Irving Weissman and Dr. Fred H. Gage and the Registrant.
10.69**	Amended and Restated Cross License Agreement dated as of October 29, 1997 between Modex Therapeutiques SA and the Registrant.
10.70	Letter Agreement dated as of September 30, 1997 between Dr. Seth Rudnick and the Registrant.
10.71****	StemCells, Inc. 1996 Stock Option Plan.
10.72****	1997 StemCells Research Stock Option Plan (the "1997 Plan").
10.73****	Form of Performance-Based Incentive Option Agreement issued under the 1997 Plan.
10.74	Employment Agreement dated as of September 25, 1997 between Dr. Richard M. Rose and the Registrant.
10.75	Employment agreement dated as of April 17, 1997, between John S. McBride and the Registrant.
10.76	Severance agreement dated as of July 21, 1997, between Dr. Sandra Nusinoff Lehrman and the Registrant.
10.77	Severance agreement dated as of July 29, 1997 between Dr. E. Edward Baetge and the Registrant.
10.78	Loan Agreement dated as of May 15, 1996 between Fleet National Bank and Registrant together with the related Promissory Note executed by Registrant and an amendatory agreement dated as of May 15, 1997.
21	Subsidiaries of the Registrant.
23.1	Consent of Ernst & Young LLP, Independent Auditors.
27	Financial Data Schedule for fiscal year ended December 31, 1997.
99	Cautionary Factors Relevant to Forward-Looking Information.

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++ Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Registration Statement on Form S-1, File No. 33-85494.

+++ Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Registration Statement on Form S-3, File No. 33-97272.

++++ Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Registration Statement on Form S-1, File No. 33-91228.

* Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, Registration Statement on Form S-1, File No. 33-45739.

Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Annual Report on Form 10-K for fiscal year ended December 31, 1992 and filed March 30, 1993.

** Confidential treatment requested as to certain portions. The term "confidential treatment" and the mark "**" as used throughout the indicated Exhibits mean that material has been omitted and separately filed with the Commission.

Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 1994 and filed on May 14, 1994.

+ Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1993 and filed on March 30, 1994.

! Previously filed with the Commission as an Exhibit to and incorporated by reference to, the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 1996.

!! Previously filed with the Commission as an Exhibit to and incorporated by reference to, the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1996.

!!! Previously filed with the Commission as an Exhibit to, and incorporated herein by reference to, the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1996 and filed on March 31, 1997.

!!!! Previously filed with the Commission as an Exhibit to, and incorporated herein by reference to, the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1995.

*** Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1997 and filed on November 14, 1997.

**** Previously filed with the Commission as Exhibits to, and incorporated herein by reference to, the Registrant's Registration Statement on Form S-8, File No. 333-37313.

(b) CURRENT REPORTS ON FORM 8-K.

On October 7, 1997, the Company filed a Report on Form 8-K with the Securities and Exchange Commission describing the StemCells, Inc. arrangements. See "Subsidiary--StemCells, Inc."

SIGNATURES

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

CYTOTHERAPEUTICS, INC.

BY: /S/ RICHARD M. ROSE, M.D.
Richard M. Rose, M.D.
President and Chief Executive Officer

Dated: March 30, 1998

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

SIGNATURE	CAPACITY	DATE
/s/ RICHARD M. ROSE, M.D. Richard M. Rose, M.D.	President, Chief Executive Officer, and Director (principal executive officer)	March 30, 1998
/s/ JOHN S. MCBRIDE John S. McBride	Chief Financial Officer and Treasurer (principal financial and accounting officer); Senior Vice President, Business Operations	March 30, 1998
/s/ PATRICK AEBISCHER, M.D., PH.D. Patrick Aebischer, M.D., Ph.D.	Director	March 30, 1998
/s/ EDWIN C. CADMAN, M.D. Edwin C. Cadman, M.D.	Director	March 30, 1998
/s/ DONALD R. CONKLIN Donald R. Conklin	Director	March 30, 1998
/s/ MARK J. LEVIN Mark J. Levin	Director	March 30, 1998
/s/ SETH A. RUDNICK, M.D. Seth A. Rudnick, M.D.	Chairman of the Board	March 30, 1998
/s/ RICHARD J. RAMSDEN Richard J. Ramsden	Director	March 30, 1998
/s/ PETER K. SIMON Peter K. Simon	Director	March 30, 1998
/s/ IRVING L. WEISSMAN, M.D. Irving L. Weissman, M.D.	Director	March 30, 1998

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CAUTIONARY FACTORS RELEVANT TO FORWARD-LOOKING INFORMATION

CYTOTHERAPEUTICS, INC. (THE "COMPANY") WISHES TO CAUTION READERS THAT THE FOLLOWING IMPORTANT FACTORS, AMONG OTHERS, IN SOME CASES HAVE AFFECTED AND IN THE FUTURE COULD AFFECT THE COMPANY'S RESULTS AND COULD CAUSE ACTUAL RESULTS AND NEEDS OF THE COMPANY TO VARY MATERIALLY FROM FORWARD-LOOKING STATEMENTS MADE IN THIS ANNUAL REPORT BY THE COMPANY ON THE BASIS OF MANAGEMENT'S CURRENT EXPECTATIONS. THE BUSINESS IN WHICH THE COMPANY IS ENGAGED IS RAPIDLY CHANGING, EXTREMELY COMPETITIVE AND INVOLVES A HIGH DEGREE OF RISK, AND ACCURACY WITH RESPECT TO FORWARD-LOOKING PROJECTIONS IS DIFFICULT.

EARLY STAGE DEVELOPMENT; HISTORY OF OPERATING LOSSES -- Substantially all of the Company's revenues to date have been derived, and for the foreseeable future substantially all of the Company's revenues will be derived, from collaborative agreements, research grants and income earned on invested funds. The Company will incur substantial operating losses in the future as the Company conducts its research, development, clinical trial and manufacturing activities. There can be no assurance that the Company will achieve revenues from product sales or become profitable.

FUTURE CAPITAL NEEDS; UNCERTAINTY OF ADDITIONAL FUNDING -- The development of the Company's products will require the commitment of substantial resources to conduct the time-consuming research, preclinical development and clinical trials that are necessary for regulatory approvals and to establish production and marketing capabilities, if such approvals are obtained. The Company will need to raise substantial additional funds to continue its product development efforts and intends to seek such additional funds through partnership, collaborative or other arrangements with corporate sponsors, public or private equity or debt financings, or from other sources. Future cash requirements may vary from projections based on changes in the Company's research and development programs, progress in preclinical and clinical testing, the Company's ability to enter into, and perform successfully under, collaborative agreements, competitive and technological advances, the need to obtain proprietary rights owned by third parties, facilities requirements, changes in regulations and other factors. Lack of necessary funds may require the Company to delay, reduce or eliminate some or all of its research and product development programs or to license its potential products or technologies to third parties. No assurance can be given that funding will be available when needed, if at all, or on terms acceptable to the Company.

UNCERTAINTIES OF CLINICAL DEVELOPMENT AND NEW MODE OF THERAPY -- None of the Company's proposed products has been approved for commercial sale or entered Phase III clinical trials. Even if the Company's proposed products appear to be promising at an early stage of research or development such products may later prove to be ineffective, have adverse side effects, fail to receive necessary regulatory approvals, be difficult or uneconomical to manufacture or market on a commercial scale, be adversely affected by government price controls or limitations on reimbursement, be precluded from commercialization by proprietary rights of third parties, by regulatory restrictions, or be subject to significant competition from other products. There can be no assurance that the Company will be able to demonstrate, as required, that its implants, on a consistent basis and on a commercial scale, among other things: (i) successfully isolate transplanted cells from the recipient's immune system; (ii) remain biocompatible with the tissue into which they are implanted, including, for certain implants, brain tissue; (iii) adequately maintain the viability of cells contained within the membrane for a sufficiently long time to be efficacious and commercially viable; (iv) safely permit the therapeutic substances produced by the cells within the membrane to pass through the membrane unto the patient in controlled doses for extended periods; and (v) are sufficiently durable for the intended indication. While clinicians have generally had little difficulty in retrieving the Company's implants, there have been cases where the implant broke on attempted explant. The Company has changed its implantation procedure and its implants and is continuing a program of developing stronger implants. In addition, the viability of implanted encapsulated cells varies depending of the cell type, the implantation location and other factors. Lack of viability could restrict certain of the Company's programs to indications

where long-term delivery of the therapeutics substances is not required. There can also be no assurance that the products that may be generated in the Company's stem cell programs will: (i) survive and persist in the desired locations, (ii) provide the therapeutic benefits intended, (iii) properly differentiate and integrate into existing tissue in the desired manner, or (iv) not cause tumors or other side effects.

There has been increasing regulatory concern about the risks of cell transplantation. Concern has focused on the use of cells derived from cows (such as are used in the Company's pain program) and cells from primates and pigs. The United Kingdom has adopted a moratorium on xenotransplantation pending further research and discussion; the EC Commission has introduced a ban on the use of "high-risk material" from cattle and sheep in the Member States of the European Union in the manufacture of pharmaceuticals (this ban would apparently not include the type of cells used in the Company's pain program). In addition, the FDA has proposed guidelines which impose significant constraints on the conduct of clinical trials utilizing xenotransplantion and are likely to significantly affect the cost of producing the Company's products using nonhuman cells; such costs could make the Company's products cost more to produce than the Company receives for their production. Furthermore, the FDA has published a "Proposed Approach to Regulation of Cellular and Tissue-Based Products" which relates to the use of human cells. The Company cannot presently determine the effects of such actions nor what other actions might be taken. Restrictions on the testing or use of cells, whether human or nonhuman, as human therapeutics, could adversely affect the Company's product development programs and the Company itself. See "Government Regulation."

DEPENDENCE ON OUTSIDE PARTIES -- The Company's strategy for the research, development, commercialization and marketing of its products contemplates that the Company will enter into various arrangements with corporate sponsors, pharmaceutical companies, universities, research groups and others. There is no assurance that the Company will be able to enter into any additional arrangements on terms acceptable to the Company, or successfully perform its obligations under its existing or any additional arrangements. If any of the Company's collaborators fails to perform its obligations in a timely manner or terminate their agreement with the Company, the development or commercialization of the Company's product candidate or research program under such collaborative agreement may be adversely affected. Moreover, the Company is particularly dependent on its pain program partner, Astra AB, because changes in the development of this particular program may significantly affect the Company's stock price. In addition, because of the Company's obligation to repurchase certain of the stock it sold to Genentech in connection with certain terminations of the Parkinson's Agreement, any such termination could have an adverse effect on the Company's liquidity.

NEED FOR AND UNCERTAINTY OF OBTAINING PATENT PROTECTION -- Patent protection for products such as those the Company proposes to develop is highly uncertain and involves complex factual and evolving legal questions. No assurance can be given that any patents issued or licensed to the Company will not be challenged, invalidated or circumvented, or that the rights granted under such patents will provide competitive advantages to the Company.

EXISTENCE OF THIRD PARTY PATENTS AND PROPRIETARY RIGHTS; NEED TO OBTAIN LICENSE -- A number of pharmaceutical, biotechnology and other companies, universities and research institutions have filed patent applications or have been issued patents relating to cell therapy and encapsulation and other technologies potentially relevant to or required by the Company's expected products. The Company cannot predict which, if any, of such applications will issue as patents or the claims which might be allowed. The Company is aware that a number of entities have filed applications relating to stem and/or progenitor cells. The Company is also aware of a number of third-party patent applications and patents relating to cell encapsulation or claiming use of genetically modified cells to treat disease, disorder or injury. In particular, the Company is aware of a third-party U.S. patent which relates the use of cells for alleviating chronic pain in humans and of two issued U. S. patents claiming certain methods for treating defective, diseased or damaged cells in the mammalian CNS by grafting genetically modified cells. The Company cannot predict

the effect of existing patent applications and patents on future unencapsulated products. In addition, the Company is aware of third-party patents and patent applications claiming rights to the neurotrophic factors (such as CNTF, NT 4/5, Neurturin, and CT-1) which the Company hopes to deliver with its technology, and to the production of these factors through the use of genetically modified cells. The Company expects to use genetically modified cells to produce these factors for use in its encapsulated products and expects that it may wish to genetically modify its stem/progenitor cells. The Company may also be required to seek licenses in regard to other cell lines, the techniques used in creating, obtaining or maintaining such cell lines, the materials used in the manufacture of its implants or otherwise. There can be no assurance that the Company will be able to establish collaborative arrangements or obtain licenses to the foregoing technology or to other necessary or desirable technology on acceptable terms, if at all, or that the patents underlying any such licenses will be valid and enforceable. See "Patents, Proprietary Rights and Licenses" in the Company's Annual Report on Form 10-K.

GOVERNMENT REGULATION -- The Company's research, preclinical development and clinical trials, as well as the manufacturing and marketing of its potential products, are subject to extensive regulation by governmental authorities in the United States and other countries. The process of obtaining FDA and other required regulatory approvals is lengthy, expensive and uncertain. There can be no assurance that the Company or its collaborators will be able to obtain the necessary approvals to commence or continue clinical testing or to manufacture or market its potential products in anticipated time frames, if at all. In addition, several legislative proposals have been made to reform the FDA. If such proposals are enacted they may result in significant changes in the regulatory environment the Company faces. These changes could result in different, more costly or more time consuming approval requirements for the Company's products, in the dilution of FDA resources available to review the Company's products, or in other unpredictable consequences. See "Government Regulation" in the Company's Annual Report on Form 10-K.

SOURCES OF CELLS AND OTHER MATERIALS -- The Company's potential products require genetically engineered cell lines or living cells harvested from animal or human sources. There can be no assurance that the Company will successfully identify or develop sources of the cells required for its potential products and obtain such cells in quantities sufficient to satisfy the commercial requirements of its potential products. These supply limitations may apply, in particular, to primary cells which must be drawn directly from animal or human sources, such as the bovine adrenal chromaffin cells currently used in the Company's product for the treatment of pain. As an alternative to primary cells, the Company is developing products based on the use of genetically altered cells. Intellectual property rights to important genetic constructs used in developing such cells, including the constructs used to develop cells producing neurotrophic factors, are or may be claimed by one or more companies, which could prevent the Company from using such cells. In addition, many suppliers of materials used by the Company in its media, implants, and other components have restricted the use of such materials for implantation into humans; if the Company cannot obtain the necessary materials for its implants, the Company would be adversely affected.

MANUFACTURING UNCERTAINTIES -- The Company's pilot manufacturing plant, may not have sufficient capacity to permit the Company to produce all the products for all of the clinical trials it anticipates developing. In addition, the Company has not developed the capability to commercially manufacture any of its proposed products and is unaware of any other company which has manufactured any membrane-encapsulated cell product on a commercial scale. There can be no assurance that the Company will be able to develop the capability of manufacturing any of its proposed products at a cost or in the quantities necessary to make a commercially viable product, if at all.

COMPETITION -- Competitors of the Company are numerous and include major pharmaceutical and chemical companies, biotechnology companies, universities and other research institutions. Currently, several of these competitors market and sell therapeutic products for the treatment of chronic pain, Parkinson's disease and other CNS conditions. In addition, most of the Company's competitors have

substantially greater capital resources, experience in obtaining regulatory approvals and, in the case of commercial entities, experience in manufacturing and marketing pharmaceutical products, than the Company. A number of other companies are attempting to develop methods of delivering therapeutic substances within or across the blood brain barrier. There can be no assurance that the Company's competitors will not succeed in developing technologies and products that are more effective than those being developed by the Company or that would render the Company's technology and products obsolete or non-competitive. See "Competition" in the Company's Annual Report on Form 10-K.

DEPENDENCE ON KEY PERSONNEL -- The Company is highly dependent on the principal members of its management and scientific staff and certain of its outside consultants. Loss of the services of any of these individuals could have a material adverse effect on the Company's operations. In addition, the Company's operations are dependent upon its ability to attract and retain additional qualified scientific and management personnel. There can be no assurance the Company will be able to attract and retain such personnel on acceptable terms given the competition among pharmaceutical, biotechnology and health care companies, universities and research institutions for experienced personnel.

REIMBURSEMENT AND HEALTH CARE REFORM -- In both domestic and foreign markets, sales of the Company's potential products will depend in part upon the availability and amounts of reimbursement from third-party health care payor organizations, including government agencies, private health care insurers and other health care payors such as health maintenance organizations and self-insured employee plans. There is considerable pressure to reduce the cost of therapeutic products. There can be no assurance that reimbursement will be provided by such payors at all or without substantial delay, or, if such reimbursement is provided, that the approved reimbursement amounts will provide sufficient funds to enable the Company to sell its products on a profitable basis. See "Reimbursement and Health Cost Control" in the Company's Annual Report on Form 10-K.

SCHEDULE II

VALUATION AND QUALIFYING ACCOUNTS

	BALANCE AT BEGINNING OF YEAR	ADDITIONS: CHARGED TO COSTS AND EXPENSES	ADDITIONS: CHARGED TO OTHER ACCOUNTS	DEDUCTIONS	BALANCE AT END OF YEAR
Year Ended Dec. 31 1997:					
Other Investments, net	$2,330,848	0	0	0	$2,330,848
Year Ended Dec. 31, 1996:					
Other Investments, net	$2,330,848	0	0	0	$2,330,848
Year Ended Dec. 31, 1995:					
Other Investments, net	0	$2,330,848	0	0	$2,330,848

EXHIBIT INDEX

EXHIBIT NO.	DESCRIPTION
10.58	Lease Agreement dated as of November 21, 1997 by and between Hub RI Properties Trust, as Landlord, and CytoTherapeutics, Inc., as Tenant
10.68	Letter Agreement between each of Dr. Irving Weissman and Dr. Fred H. Gage and the Registrant
10.69	Amended and Restated Cross License Agreement dated as of October 29, 1997 between Modex Therapeutiques SA and the Registrant
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10.77	Severance agreement dated as of July 29, 1997 between Dr. E. Edward Baetge and the Registrant

10.78	Loan Agreement dated as of May 15, 1996 between Fleet National Bank and Registrant together with the related Promissory Note and an amendatory agreement dated as of May 15, 1997
21	Subsidiaries of the Registrant
23.1	Consent of Ernst & Young LLP, Independent Auditors
27	Financial Data Schedule for fiscal year ended December 31, 1997
99	Cautionary Factors Relevant to Forward Looking Statements

EXHIBIT 10.58

LEASE AGREEMENT

DATED AS OF NOVEMBER 21, 1997

BY AND BETWEEN

HUB RI PROPERTIES TRUST,
AS LANDLORD,

AND

CYTOTHERAPEUTICS, INC.,
AS TENANT

TABLE OF CONTENTS

ARTICLE 1

MASTER LEASE AGREEMENT

THIS LEASE AGREEMENT is entered into as of this __ day of November, 1997, by and between Hub RI Properties Trust, a Maryland real estate investment trust, having its principal office at 400 Centre Street, Newton, Massachusetts 02158, as landlord ("LANDLORD"), and Cytotherapeutics, Inc., a Delaware corporation, having its principal office at 701 George Washington Highway, Lincoln, Rhode Island 02865, as tenant ("TENANT").

W I T N E S S E T H:

WHEREAS, Landlord, on the date hereof, has acquired fee simple title to the Property (this and other capitalized terms used and not otherwise defined herein having the meanings ascribed to such terms in ARTICLE 1); and

WHEREAS, Landlord wishes to lease the Property to Tenant and Tenant wishes to lease the Property from Landlord, all subject to and upon the terms and conditions herein set forth;

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

ARTICLE 1
DEFINITIONS

For all purposes of this Agreement, except as otherwise expressly provided or unless the context otherwise requires, (i) the terms defined in this Article shall have the meanings assigned to them in this Article and include the plural as well as the singular, (ii) all accounting terms not otherwise defined herein shall have the meanings assigned to them in accordance with GAAP, (iii) all references in this Agreement to designated "Articles," "Sections" and other subdivisions are to the designated Articles, Sections and other subdivisions of this Agreement, and (iv) the words "herein," "hereof," "hereunder" and other words of similar import refer to this Agreement as a whole and not to any particular Article, Section or other subdivision.

1.1 "ADDITIONAL RENT" shall have the meaning given such term in SECTION 3.1.2.

1.2 "ADJUSTED PURCHASE PRICE" shall mean $8,000,000, plus any other amount disbursed or advanced by Landlord to finance, or to reimburse Tenant for its financing of, any Capital Addition to the Property less the amount of any Award or the proceeds of any insurance received by Landlord in connection with a partial Condemnation or a partial casualty involving the Property as described in SECTION 11.2 or 10.2.2, and not applied by Landlord to the restoration of the Leased Property as provided therein.

1.3 "AFFILIATED PERSON" shall mean, with respect to any Person, (a) in the case of any such Person which is a partnership, any partner in such partnership, (b) in the case of any such Person which is a limited liability company, any member of such company, (c) any other Person which is a Parent, a Subsidiary, or a Subsidiary of a Parent with respect to such Person or to one or more of the Persons referred to in the preceding clauses (a) and (b), (d) any other Person who is an officer, director, trustee or employee of, or partner in, such Person or any Person referred to in the preceding clauses (a), (b) and (c), and (e) any other Person who is a member of the Immediate Family of such Person or of any Person referred to in the preceding clauses (a) through (d).

1.4 "AGREEMENT" shall mean this Lease Agreement, including EXHIBITS A THROUGH C hereto, as it and they may be amended from time to time as herein provided.

1.5 "APPLICABLE LAWS" shall mean all applicable laws, statutes, regulations, rules, ordinances, codes, licenses, permits and orders (whether now existing or hereafter enacted or promulgated irrespective of whether its enactment is foreseeable or contemplated), of all courts of competent jurisdiction and

Government Agencies, and all applicable judicial and administrative and regulatory decrees, judgments and orders, including common law rulings and determinations, relating to injury to, or the protection of, real or personal property or human health (except those requirements which, by definition, are solely the responsibility of employers) or the Environment, including, without limitation, all valid and lawful requirements of courts and other Government Agencies pertaining to reporting, licensing, permitting, investigation, remediation and removal of underground improvements (including, without limitation, treatment or storage tanks, or water, gas or oil wells), or emissions, discharges, releases or threatened releases of Hazardous Substances, chemical substances, pesticides, petroleum or petroleum products, pollutants, contaminants or hazardous or toxic substances, materials or wastes whether solid, liquid or gaseous in nature, into the Environment, or relating to the manufacture, processing, distribution, use, treatment, storage, disposal, transport or handling of Hazardous Substances or Regulated Medical Wastes, underground improvements (including, without limitation, treatment or storage tanks, or water, gas or oil wells), or pollutants, contaminants or hazardous or toxic substances, materials or wastes, whether solid, liquid or gaseous in nature.

1.6 "AWARD" shall mean all compensation, sums or other value awarded, paid or received by virtue of a total or partial Condemnation of the Property (after deduction of all reasonable legal fees and other reasonable out-of-pocket costs and expenses, including, without limitation, expert witness fees, incurred by Landlord, in connection with obtaining any such award).

1.7 "BUSINESS DAY" shall mean any day other than Saturday, Sunday, or any other day on which banking institutions in the State are authorized by law or executive action to close.

1.8 "CAPITAL ADDITION" shall mean one or more new buildings, structures or the material expansion of existing improvements or structures, which are constructed on any parcel or portion of the Land.

1.9 "CAPITAL ADDITIONS COST" shall mean the cost of any Capital Addition proposed to be made by Tenant at the Property, whether paid for by Tenant or Landlord.

1.10 "CHANGE IN CONTROL" shall mean the acquisition by any Person, or two or more Persons acting in concert, of beneficial ownership (within the meaning of Rule 13d-3 of the SEC) of 51% or more, or rights, options or warrants to acquire 51% or more, of the outstanding shares of voting stock of Tenant or the merger or consolidation of Tenant with or into any other Person or any one or more sales or conveyances to any Person of all or substantially all of the assets of Tenant.

1.11 "CODE" shall mean the Internal Revenue Code of 1986 and, to the extent applicable, the Treasury Regulations promulgated thereunder, each as from time to time amended.

1.12 "COMMENCEMENT DATE" shall mean the date of this Agreement.

1.13 "CONDEMNATION" shall mean (a) the exercise of any governmental power with respect to the Property, whether by legal proceedings or otherwise, by a Condemnor of its power of condemnation; (b) a voluntary sale or transfer of the Property by Landlord to any Condemnor, either under threat of condemnation or while legal proceedings for condemnation are pending; and (c) a taking or voluntary conveyance of all or part of the Property, or any interest therein, or right accruing thereto or use thereof, as the result or in settlement of any condemnation or other eminent domain proceeding affecting the Property, whether or not the same shall have actually been commenced.

1.14 "CONDEMNOR" shall mean any public or quasi-public authority, or private corporation or individual, having the power of Condemnation.

1.15 "CONSOLIDATED FINANCIALS" shall mean, for any Fiscal Year or other accounting period of Tenant and its consolidated subsidiaries, annual audited and quarterly unaudited financial statements prepared on a consolidated basis (if required by GAAP), including Tenant's consolidated balance sheet and the related statements of income and cash flows, all in reasonable detail, and setting forth in comparative form the

corresponding figures for the corresponding period in the preceding Fiscal Year, and prepared in accordance with GAAP throughout the periods reflected.

1.16 "DATE OF TAKING" shall mean the date the Condemnor has the right to possession of the Property, or any portion thereof, in connection with a Condemnation.

1.17 "DECLARATION" shall mean the Declaration of Trust establishing Landlord, dated November 3, 1997, as amended and restated from time to time.

1.18 "DEFAULT" shall mean any event or condition which with the giving of notice and/or lapse of time may ripen into an Event of Default.

1.19 "ENCUMBRANCE" shall have the meaning given such term in SECTION 21.1.

1.20 "ENTITY" shall mean any general partnership, limited partnership, limited liability company or partnership, corporation, joint venture, trust, business trust, cooperative or association or any Governmental Agencies.

1.21 "ENVIRONMENT" shall mean soil, surface waters, ground waters, land, stream, sediments, surface or subsurface strata and ambient air.

1.22 "ENVIRONMENTAL OBLIGATION" shall have the meaning given such term in SECTION 4.3.1.

1.23 "ENVIRONMENTAL NOTICE" shall have the meaning given such term in SECTION 4.3.1.

1.24 "ENVIRONMENTAL REPORT" shall have the meaning given such term in SECTION 4.3.2.

1.25 "EVENT OF DEFAULT" shall have the meaning given such term in SECTION 12.1.

1.26 "EXTENDED TERMS" shall have the meaning given such term in SECTION 2.4.

1.27 "FACILITY" shall mean the buildings (including a rehabilitated building and a newly constructed addition comprising, collectively, approximately 64,934 square feet of gross interior space and approximately 62,000 square feet of net rentable space) and improvements located on the Land, as the same may be altered in accordance with the terms hereof.

1.28 "FACILITY MORTGAGE" shall mean any Encumbrance placed upon the Property in accordance with ARTICLE 21.

1.29 "FACILITY MORTGAGEE" shall mean the holder of any Facility Mortgage.

1.30 "FAIR MARKET RENTAL" shall mean the rental which a willing tenant not compelled to rent would pay a willing landlord not compelled to lease for the use and occupancy of the Property (including all Capital Additions other than Tenant's Capital Additions) on the terms and conditions of this Agreement for the term in question, assuming Tenant is not in default hereunder and determined by agreement between Landlord and Tenant or, failing agreement, in accordance with the appraisal procedures set forth in ARTICLE 19.

1.31 "FAIR MARKET VALUE" shall mean the price that a willing buyer not compelled to buy would pay a willing seller not compelled to sell for the Property (without taking into account any reduction in value resulting from any indebtedness to which the Property is subject), assuming the same is unencumbered by this Agreement and determined by agreement between Landlord and Tenant or, failing agreement, the appraisal procedures set forth in ARTICLE 19.

1.32 "FINANCIAL OFFICER'S CERTIFICATE" shall mean, as to any Person, a certificate of the chief financial officer of such Person, duly authorized, accompanying the financial statements required to be delivered by such Person pursuant to SECTION 17.2, in which such officer shall certify (a) that, to such officer=s knowledge, such statements have been properly prepared in accordance with GAAP and are true, correct and complete in all material respects and fairly present the financial condition of such Person at and as of

the dates thereof and the results of its and their operations for the periods covered thereby, and (b) that such officer has reviewed this Agreement and, to such officer=s knowledge, has no knowledge of any Default or Event of Default hereunder.

1.33 "FISCAL YEAR" shall mean the twelve (12) month period from January 1 to December 31.

1.34 "FIXED TERM" shall have the meaning given such term in SECTION 2.3.

1.35 "FIXTURES" shall have the meaning given such term in SECTION 2.1(D).

1.36 "GAAP" shall mean generally accepted accounting principles consistently applied.

1.37 "GOVERNMENT AGENCIES" shall mean any court, agency, authority, board (including, without limitation, environmental protection, planning and zoning), bureau, commission, department, office or instrumentality of any nature whatsoever of any governmental or quasi-governmental unit of the United States or the State or any county or any political subdivision of any of the foregoing, whether now or hereafter in existence, having jurisdiction over Tenant or the Property or any portion thereof or the Facility operated thereon.

1.38 "HAZARDOUS SUBSTANCES" shall mean any substance:

(a) the presence of which requires or may hereafter require notification, investigation or remediation under any federal, state or local statute, regulation, rule, ordinance, order, action or policy; or

(b) which is or becomes defined as a "hazardous waste", "hazardous material" or "hazardous substance" or "pollutant" or "contaminant" under any present or future federal, state or local statute, regulation, rule or ordinance or amendments thereto including, without limitation, the Comprehensive Environmental Response, Compensation and Liability Act (42 U.S.C. ET SEQ.) and the Resource Conservation and Recovery Act (42 U.S.C. section 6901 ET SEQ.) and the regulations promulgated thereunder; or

(c) which is toxic, explosive, corrosive, flammable, infectious, radioactive, carcinogenic, mutagenic or otherwise hazardous and is or becomes regulated by any governmental authority, agency, department, commission, board, agency or instrumentality of the United States, any state of the United States, or any political subdivision thereof; or

(d) the presence of which on the Property causes or threatens to cause a violation of Applicable Laws or poses or threatens to pose a hazard to the Property or to the health or safety of persons on or about the Property; or

(e) without limitation, which contains gasoline, diesel fuel or other petroleum hydrocarbons or volatile organic compounds; or

(f) without limitation, which contains polychlorinated biphenyls (PCBs) or asbestos or urea formaldehyde foam insulation; or

(g) without limitation, which contains or emits radioactive particles, waves or material; or

(h) without limitation, constitutes Regulated Medical Wastes.

1.39 "IMMEDIATE FAMILY" shall mean, with respect to any individual, such individual's spouse, parents, brothers, sisters, children (natural or adopted), stepchildren, grandchildren, grandparents, parents-in-law, brothers-in-law, sisters-in-law, nephews and nieces.

1.40 "IMPOSITIONS" shall mean, collectively, all taxes (including, without limitation, all taxes imposed under the laws of the State, as such laws may be amended from time to time, and all ad valorem, sales and use, single business, gross receipts, transaction privilege, rent or similar taxes as the same relate to or are imposed upon Landlord, Tenant or the business conducted upon the Property), assessments (including,

without limitation, all assessments for public improvements or benefit, whether or not commenced or completed prior to the date hereof and whether or not to be completed within the Term), water, sewer or other rents and charges, excises, tax levies, fees (including, without limitation, license, permit, inspection, authorization and similar fees) and all other governmental charges, in each case whether general or special, ordinary or extraordinary, or foreseen or unforeseen, of every character in respect of the Property or the business conducted thereon by Tenant (including all interest and penalties thereon due to any failure in payment by Tenant), which at any time prior to, during or in respect of the Term hereof may be assessed or imposed on or in respect of or be a lien upon (a) the Property or any part thereof or any rent therefrom or any estate, right, title or interest therein, or (b) any occupancy, operation, use or possession of, or sales from, or activity conducted on, or in connection with the Property or the leasing or use of the Property or any part thereof by Tenant; PROVIDED, HOWEVER, that nothing contained herein shall be construed to require Tenant to pay (i) any tax based on income imposed on Landlord, (ii) any revenue tax of Landlord, (iii) any transfer fee or other tax imposed with respect to the sale, exchange or other disposition by Landlord of the Property or the proceeds thereof (other than in connection with the sale, exchange or other disposition to, or in connection with a transaction involving, Tenant), or (iv) any single business, gross receipts (other than a tax on any rent received by Landlord from Tenant), transaction privilege, rent or similar taxes as the same relate to or are imposed upon Landlord, except to the extent that any tax, assessment, tax levy or charge, which Tenant is obligated to pay pursuant to the first sentence of this definition and which is in effect at any time during the Term hereof is totally or partially repealed, and a tax, assessment, tax levy or charge set forth in clause (i) or (ii) preceding is levied, assessed or imposed expressly in lieu thereof.

1.41 "INDEBTEDNESS" shall mean all obligations, contingent or otherwise, which in accordance with GAAP should be reflected on the obligor's balance sheet as liabilities.

1.42 "INSURANCE REQUIREMENTS" shall mean all terms of any insurance policy required by this Agreement and all requirements of the issuer of any such policy.

1.43 "LAND" shall have the meaning given such term in SECTION 2.1(A).

1.44 "LANDLORD" shall have the meaning given such term in the preambles to this Agreement.

1.45 "LEASE YEAR" shall mean each calendar year, or portion thereof, during the term, commencing with the 1997 calendar year.

1.46 "IMPROVEMENTS" shall have the meaning given such term in SECTION 2.1(B).

1.47 "LEGAL REQUIREMENTS" shall mean all Applicable Laws and (a) all permits, licenses, certificates of need, authorizations and regulations necessary to operate the Property for its Primary Intended Use, and (b) all covenants, agreements, restrictions and encumbrances contained in any instruments at any time in force affecting the Property, including those (i) which may require material repairs, modifications or alterations in or to the Property or (ii) with respect to which a violation thereof would in any way adversely affect the use and enjoyment thereof.

1.48 "LENDING INSTITUTION" shall mean any insurance company, federally insured commercial or savings bank, national banking association, savings and loan association, employees' welfare, pension or retirement fund or system, corporate profit sharing or pension trust, college or university, or real estate investment trust, including any corporation qualified to be treated for federal tax purposes as a real estate investment trust, such trust having a net worth of at least $100,000,000.

1.49 "LIEN" shall mean any mortgage, security interest, pledge, collateral assignment, or other encumbrance, lien or charge of any kind, or any transfer of any property or assets for the purpose of subjecting the same to the payment of Indebtedness or performance of any other obligation in priority to payment of its general creditors.

1.50 "MINIMUM RENT" shall mean the respective monthly amounts set forth in EXHIBIT B.

1.51 "NOTICE" shall mean a notice given in accordance with SECTION 23.12.

1.52 "OFFICER'S CERTIFICATE" shall mean a certificate signed by an officer of Tenant who has been duly authorized by the board of directors of Tenant.

1.53 "OVERDUE RATE" shall mean, on any date, a PER ANNUM rate of interest equal to the lesser of 5% over the Prime Rate or the maximum rate allowed by law. "PRIME RATE" shall mean the annual floating rate of interest, determined daily and expressed as a percentage from time to time, announced by the largest national or state-chartered banking institution in Rhode Island which announces a "prime" or "base" rate. If at any time no national or state-chartered banking institution having its principal offices in Rhode Island is announcing such a floating rate, "PRIME RATE" shall mean a rate of interest, determined daily, which is two (2) percentage points above the 14-day moving average closing trading price of 90-day Treasury Bills.

1.54 "PARENT" shall mean, with respect to any Person, any Person which owns directly, or indirectly through one or more Subsidiaries or Affiliated Persons, fifty-one percent (51%) or more of the voting or beneficial interest in, or otherwise has the right or power (whether by contract, through ownership of securities or otherwise) to control, such Person.

1.55 "PERMITTED ENCUMBRANCES" shall mean all rights, restrictions, and easements of record set forth on Schedule B to the applicable owner's title insurance policy issued to Landlord on the date hereof, and a notice or memorandum relating to this Lease.

1.56 "PERMITTED LIENS" shall mean any Liens granted in accordance with SECTION 22.9.

1.57 "PERSON" shall mean any individual or Entity, and the heirs, executors, administrators, legal representatives, successors and assigns of such Person where the context so admits.

1.58 "PRIMARY INTENDED USE" shall have the meaning given such term in SECTION 4.1.1.

1.59 "PROPERTY" shall have the meaning given such term in SECTION 2.1.

1.60 "QUALIFIED APPRAISER" shall mean an appraiser who is not in control of, controlled by or under common control with either Landlord or Tenant and has not been an employee of Landlord or Tenant or any Affiliated Person with respect to either of Landlord or Tenant at any time during the ten (10) year period preceding the relevant date, who is qualified to appraise commercial real estate in the State and is a member of the American Institute of Real Estate Appraisers (or any successor association or body of comparable standing if such Institute is not then in existence) and who has held his or her certificate as an M.A.I. or its equivalent for a period of not less than three (3) years, and has been actively engaged in the appraisal of commercial real estate in such area for a period of not less than five (5) years, immediately preceding his or her appointment hereunder.

1.61 "REGULATED MEDICAL WASTES" shall mean all materials generated or used on the Property by Tenant, subtenants, patients, occupants or the operators of the Property which are now or may hereafter be subject to regulation pursuant to the Material Waste Tracking Act of 1988, or any Applicable Laws.

1.62 "RENT" shall mean, collectively, the Minimum Rent, and Additional Rent.

1.63 "SEC" shall mean the Securities and Exchange Commission.

1.64 "SECURITY DEPOSIT" shall mean $750,000.

1.65 "STATE" shall mean the State of Rhode Island.

1.66 "SUBORDINATED CREDITOR" shall mean any creditor of Tenant which is a party to a Subordination Agreement in favor of Landlord.

1.67 "SUBORDINATION AGREEMENT" shall mean any agreement executed by a Subordinated Creditor pursuant to which the payment and performance of Tenant's obligations to such Subordinated Creditor are subordinated to the payment and performance of Tenant's obligations to Landlord under this Agreement.

1.68 "SUBSIDIARY" shall mean, with respect to any Person, any Entity (a) in which such Person owns directly, or indirectly through one or more Subsidiaries, more than fifty percent (50%) of the voting or beneficial interest or (b) which such Person otherwise has the right or power to control (whether by contract, through ownership of securities or otherwise).

1.69 "TANGIBLE NET WORTH" shall mean the excess of total assets (excluding the Security Deposit) over total liabilities computed in accordance with GAAP, less all intangible assets and deferred charges, including, without limitation, goodwill, debt discount, organization expenses, trademarks and trade names, patents, deferred product development costs and similar items, also so in accordance with GAAP.

1.70 "TENANT" shall have the meaning given such term in the preambles to this Agreement.

1.71 "TENANT'S CAPITAL ADDITIONS" shall have the meaning given such term in SECTION 6.2.2.

1.72 "TENANT'S PERSONAL PROPERTY" shall mean all motor vehicles and consumable inventory and supplies, furniture, furnishings, movable walls and partitions, equipment and machinery and all other personal property of Tenant located at the Property or used in Tenant's business at the Property as described on EXHIBIT C, including all of Tenant's trade fixtures, and all modifications, replacements, alterations and additions to such personal property installed at the expense of Tenant.

1.73 "TERM" shall mean, collectively, the Fixed Term and the Extended Terms, to the extent properly exercised pursuant to the provisions of SECTION 2.4, unless sooner terminated pursuant to the provisions of this Agreement.

1.74 "UNSUITABLE FOR ITS PRIMARY INTENDED USE" shall mean a state or condition of such Facility, such that (a) following any damage or destruction involving the Property, such Property cannot reasonably be expected to be restored to substantially the same condition as existed immediately before such damage or destruction, and as otherwise required by SECTION 10.2.4, within the period (not to exceed two (2) years following such damage or destruction) as to which loss of rents insurance is available to cover Rent due during such restoration period; or (b) as the result of a partial taking by Condemnation, such Facility cannot be operated on a commercially practicable basis for the Primary Intended Use.

1.75 "WORK" shall have the meaning given such term in SECTION 10.2.4.

ARTICLE 2
PROPERTY AND TERM

2.1 THE PROPERTY. Upon and subject to the terms and conditions hereinafter set forth, Landlord leases to Tenant and Tenant leases from Landlord all of the following (collectively, the "PROPERTY"):

(a) those certain parcels of land, as more particularly described in EXHIBIT A, attached hereto and made a part hereof (the "LAND");

(b) all buildings, structures, Fixtures and other improvements of every kind including, but not limited to, alleyways and connecting tunnels, sidewalks, utility pipes, conduits and lines (on-site and off-site), parking areas and roadways appurtenant to such buildings and structures presently situated upon the Land and all Capital Additions other than Tenant's Capital Additions (collectively, the "IMPROVEMENTS");

(c) all easements, rights and appurtenances relating to the Land and the Improvements; and

(d) all equipment, machinery, fixtures, and other items of property, now or hereafter permanently affixed to or incorporated into the Improvements, including, without limitation, all furnaces, boilers, heaters, electrical equipment, heating, plumbing, lighting, ventilating, incineration, air and water pollution control, waste disposal, air-cooling and air-conditioning systems and apparatus, sprinkler systems and fire and theft protection equipment, all of which, to the maximum extent

permitted by law, are hereby deemed by the parties hereto to constitute real estate, together with all replacements, modifications, alterations and additions thereto, but specifically excluding all items included within the category of Tenant's Personal Property (collectively, the "FIXTURES").

2.2 CONDITION OF THE PROPERTY. Tenant acknowledges receipt and delivery of possession of the Property and Tenant accepts the Property in its "as is" condition, subject to the existing state of title, including all covenants, conditions, restrictions, reservations, mineral leases, easements and other matters of record or that are visible or apparent on the Property, all applicable Legal Requirements, the lien of financing instruments, mortgages and deeds of trust, and such other matters which would be disclosed by an inspection of the Property and the record title thereto or by an accurate survey thereof. TENANT REPRESENTS THAT IT OCCUPIES THE PROPERTY AND HAS FULLY INSPECTED THE PROPERTY AND ALL OF THE FOREGOING AND HAS FOUND THE CONDITION THEREOF SATISFACTORY AND IS NOT RELYING ON ANY REPRESENTATION OR WARRANTY OF LANDLORD OR LANDLORD'S AGENTS OR EMPLOYEES WITH RESPECT THERETO AND TENANT WAIVES ANY CLAIM OR ACTION AGAINST LANDLORD IN RESPECT OF THE CONDITION THEREOF. LANDLORD MAKES NO WARRANTY OR REPRESENTATION, EXPRESS OR IMPLIED, IN RESPECT OF THE PROPERTY OR ANY PART THEREOF, EITHER AS TO ITS FITNESS FOR USE, DESIGN OR CONDITION FOR ANY PARTICULAR USE OR PURPOSE OR OTHERWISE, AS TO THE QUALITY OF THE MATERIAL OR WORKMANSHIP THEREIN, LATENT OR PATENT, IT BEING AGREED THAT ALL SUCH RISKS ARE TO BE BORNE BY TENANT. To the maximum extent permitted by law, however, Landlord hereby assigns to Tenant all of Landlord's rights to proceed against any predecessor in title, as well as contractors and suppliers for breaches of warranties or representations, or for latent defects in the Property. Landlord shall fully cooperate with Tenant in the prosecution of any such claims, in Landlord's or Tenant's name, all at Tenant's sole cost and expense. Tenant shall indemnify, defend, and hold harmless Landlord from and against any loss, third-party cost, damage or liability (including reasonable attorneys' fees) incurred by Landlord in connection with such cooperation.

2.3 FIXED TERM. The initial term of this Agreement (the "FIXED TERM") shall commence on the Commencement Date and expire on June 30, 2013.

2.4 EXTENDED TERM. Tenant shall have the right to extend the Term for two consecutive ten (10) year renewal terms (collectively, the "EXTENDED TERMS").

Each Extended Term shall commence on the day succeeding the expiration of the Fixed Term or the preceding Extended Term, as the case may be. All of the terms, covenants and provisions of this Agreement shall apply to each such Extended Term, except that (i) the Minimum Rent shall be as set forth in EXHIBIT B and (ii) Tenant shall have no right to extend the Term beyond the expiration of the Extended Terms. If Tenant shall elect to exercise either of the aforesaid options, it shall do so by giving Landlord Notice thereof not later than one (1) year (and not sooner than eighteen (18) months) prior to the scheduled expiration of the then current Term of this Agreement (Fixed or Extended, as the case may be), it being understood and agreed that time shall be of the essence with respect to the giving of such Notice. If Tenant shall fail to give any such Notice, this Agreement shall automatically terminate at the end of the Term then in effect and Tenant shall have no further option to extend the Term of this Agreement. If Tenant shall give such Notice, the extension of this Agreement shall be automatically effected without the execution of any additional documents; it being understood and agreed, however, that Tenant and Landlord shall execute such documents and agreements as either party shall reasonably require to evidence the same.

ARTICLE 3
RENT

3.1 RENT. Tenant shall pay to Landlord, in lawful money of the United States of America which shall be legal tender for the payment of public and private debts, without offset, abatement, demand or deduction, Minimum Rent and Additional Rent, during the Term, except as hereinafter expressly provided. All payments to Landlord shall be made by wire transfer of immediately available federal funds or by other means acceptable to Landlord in its sole discretion. Rent for any partial month shall be prorated on a per diem basis based on the actual days in such month.

3.1.1 MINIMUM RENT. Minimum Rent shall be paid in advance on the first day of each calendar month; PROVIDED, HOWEVER, that the payment of Minimum Rent with respect to any partial month in which the Commencement Date occurs and the first full month of the Fixed Term shall be payable on the Commencement Date.

3.1.2 ADDITIONAL RENT. In addition to the Minimum Rent payable hereunder, Tenant shall pay and discharge as and when due and payable the following (collectively, "ADDITIONAL RENT"):

(a) IMPOSITIONS. Subject to ARTICLE 8 relating to Permitted Contests, Tenant shall pay, or cause to be paid, all Impositions before any fine, penalty, interest or cost (other than any opportunity cost as a result of a failure to take advantage of any discount for early payment) may be added for non-payment, such payments to be made directly to the taxing authorities where feasible, and shall promptly, upon request, furnish to Landlord copies of official receipts or other satisfactory proof evidencing such payments. If any such Imposition may, at the option of the taxpayer, lawfully be paid in installments (whether or not interest shall accrue on the unpaid balance of such Imposition), Tenant may exercise the option to pay the same (and any accrued interest on the unpaid balance of such Imposition) in installments and, in such event, subject to ARTICLE 8 relating to Permitted Contests, shall pay such installments which are due during or with respect to periods occurring during the Term as the same become due and before any fine, penalty, premium, further interest or cost may be added thereto. Landlord, at its expense, shall, to the extent required or permitted by applicable law, prepare and file all tax returns in respect of Landlord's net income, gross receipts, sales and use, single business, transaction privilege, rent, ad valorem, franchise taxes and taxes on its capital stock, and Tenant, at its expense, shall, to the extent required or permitted by applicable laws and regulations, prepare and file all other tax returns and reports in respect of any Imposition as may be required by Government Agencies. Provided no Event of Default shall have occurred and be continuing, if any refund shall be due from any taxing authority in respect of any Imposition paid by Tenant, the same shall be paid over to or retained by Tenant. Landlord and Tenant shall, upon request of the other, provide such data as is maintained by the party to whom the request is made with respect to the Property as may be necessary to prepare any required returns and reports. In the event Government Agencies classify any portion of the Property as personal property, Tenant shall file all personal property tax returns in such jurisdictions where it may legally so file. Each party shall, to the extent it possesses the same, provide the other, upon request, with cost and depreciation records necessary for filing returns for any portion of the Property so classified as personal property. Where Landlord is legally required to file personal property tax returns, Landlord shall provide Tenant with copies of assessment notices in sufficient time for Tenant to file a protest. All Impositions assessed against such personal property shall be (irrespective of whether Landlord or Tenant shall file the relevant return) paid by Tenant not later than the last date on which the same may be made without interest or penalty, subject to the provisions of ARTICLE 8 relating to Permitted Contests.

Landlord shall give prompt Notice to Tenant of all Impositions payable by Tenant hereunder of which Landlord at any time has knowledge.

(b) UTILITY CHARGES. Tenant shall pay or cause to be paid all charges for electricity, power, gas, oil, water and other utilities used in connection with the Property.

(c) INSURANCE PREMIUMS. Tenant shall pay or cause to be paid all premiums for the insurance coverage required to be maintained pursuant to ARTICLE 9.

(d) OTHER CHARGES. Tenant shall pay or cause to be paid all other amounts, liabilities and obligations which Tenant assumes or agrees to pay under this Agreement, including, without limitation, all agreements to indemnify Landlord under SECTIONS 4.4 AND 9.7.

(e) REIMBURSEMENT FOR ADDITIONAL RENT. If Tenant pays or causes to be paid property taxes or similar Additional Rent attributable to periods after the end of the Term, whether upon expiration or sooner termination of this Agreement (other than termination following an Event of Default), Tenant may, within sixty (60) days of the end of the Term, provide Notice to Landlord of its estimate of such amounts. Landlord shall promptly reimburse Tenant for all payments of such taxes and other similar Additional Rent that are attributable to any period after the Term of this Agreement (less any amounts due from, but unpaid by, Tenant hereunder). If an Event of Default has occurred, Landlord shall apply such amounts to amounts due and owing under this Agreement and to the costs of collection of the same and shall pay any excess to Tenant.

3.2 LATE PAYMENT OF RENT. If any installment of Minimum Rent, or any Additional Rent which is payable directly to Landlord, shall not be paid on its due date, Tenant shall pay Landlord, on demand, as Additional Rent, a late charge (to the extent permitted by law) computed at the Overdue Rate on the amount of such installment, from the due date of such installment to the date of payment thereof, provided however if Landlord shall give Tenant a Notice of Tenant's failure to pay any Rent when due then such late charge shall be computed at the lesser of the Overdue Rate plus four (4) percentage points or the maximum rate allowed by law. To the extent that Tenant pays any Additional Rent directly to Landlord or any Facility Mortgagee pursuant to any requirement of this Agreement, Tenant shall be relieved of its obligation to pay such Additional Rent to the Entity to which it would otherwise be due.

In the event of any failure by Tenant to pay any Additional Rent when due, Tenant shall promptly pay and discharge, as Additional Rent, every fine, penalty, interest and cost which may be added for non-payment or late payment of such items. Landlord shall have all legal, equitable and contractual rights, powers and remedies provided either in this Agreement or by statute or otherwise in the case of non-payment of the Additional Rent as in the case of non-payment of the Minimum Rent.

3.3 NET LEASE. The Minimum Rent and Additional Rent shall be absolutely net to Landlord so that this Agreement shall yield to Landlord the full amount of the installments or amounts of Minimum Rent throughout the Term, subject to any other provisions of this Agreement which expressly provide for adjustment or abatement of such Rent.

3.4 NO TERMINATION, ABATEMENT, ETC. Except as otherwise specifically provided in this Agreement, Tenant, to the maximum extent permitted by law, shall remain bound by this Agreement in accordance with its terms and shall neither take any action without the consent of Landlord to modify, surrender or terminate this Agreement, nor seek, nor be entitled to any abatement, deduction, deferment or reduction of the Rent, or set-off against the Rent, nor shall the respective obligations of Landlord and Tenant be otherwise affected by reason of (a) any damage to or destruction of the Property or any portion thereof from whatever cause or any Condemnation; (b) the lawful or unlawful prohibition of, or restriction upon, Tenant's use of the Property, or any portion thereof, or the interference with such use by any Person or by reason of eviction by paramount title; (c) any claim which Tenant may have against Landlord by reason of any default or breach of any warranty by Landlord under this Agreement; (d) any bankruptcy, insolvency, reorganization, composition, readjustment, liquidation, dissolution, winding up or other proceedings affecting Landlord or any assignee or transferee of Landlord; or (e) for any other cause whether similar or dissimilar to any of the foregoing. Tenant hereby waives all rights arising from any occurrence whatsoever,

which may now or hereafter be conferred upon it by law, to (a) modify, surrender or terminate this Agreement or quit or surrender the Property or any portion thereof; or (b) entitle Tenant to any abatement, reduction, suspension or deferment of the Rent or other sums payable or other obligations to be performed by Tenant hereunder, except as otherwise specifically provided in this Agreement. The obligations of Tenant hereunder shall be separate and independent covenants and agreements, and the Rent and all other sums payable by Tenant hereunder shall continue to be payable in all events unless the obligations to pay the same shall be terminated, modified or amended pursuant to the express provisions of this Agreement.

3.5 SECURITY DEPOSIT. Upon execution of this Agreement, Tenant shall deposit with Landlord the Security Deposit. The Security Deposit shall be held by Landlord as security for the faithful performance of all the terms of this Lease to be observed and performed by Tenant. The Security Deposit shall not be mortgaged, assigned, transferred or encumbered by Tenant and any such act on the part of Tenant shall be without force and effect and shall not be binding upon Landlord.

If the Minimum Rent or Additional Rent payable hereunder shall be overdue and unpaid or should Landlord make any payment on behalf of the Tenant, or Tenant shall fail to perform any of the terms of this Lease, then Landlord may, at its option and without notice or prejudice to any other remedy which Landlord may have on account thereof, appropriate and apply the entire Security Deposit or so much thereof as may be necessary to compensate Landlord toward the payment of Minimum Rent, Additional Rent or other sums or loss or damage sustained by Landlord due to such breach by Tenant; and Tenant shall forthwith upon demand restore the Security Deposit to the original sum deposited. Landlord shall return the Security Deposit, or so much thereof as shall have not theretofore been applied in accordance with the terms hereof, and less any amounts due from, but unpaid by, Tenant hereunder, to Tenant promptly following the expiration or earlier termination of the Term of this Agreement and the surrender of possession of the Property by Tenant to Landlord in accordance with the Terms of this Agreement. While Landlord holds the Security Deposit, Landlord shall have no obligation to pay interest on the same and shall have the right to commingle the same with Landlord's other funds. If Landlord conveys Landlord's interest in the Property, the Security Deposit, or any part thereof not previously applied, shall be turned over by Landlord to Landlord's grantee, and Tenant shall look solely to such grantee for proper application of the Security Deposit in accordance with the terms hereof. Tenant agrees that the holder of a mortgage on the Property shall not be responsible to Tenant for the return or application of the Security Deposit, whether or not it succeeds to the position of Landlord hereunder, unless such holder actually receives the Security Deposit.

ARTICLE 4
USE OF THE PROPERTY

4.1 PERMITTED USE.

4.1.1 PRIMARY INTENDED USE. Tenant shall, at all times during the Term and at any other time that Tenant shall be in possession of the Property, use the Property as laboratory and office space for research and development related to healthcare and for such other uses as may be ancillary, incidental or necessary thereto, including, without limitation, production, distribution and sale of diagnostics, vaccines, drugs, and other products (any such use, together with any change as to which Landlord shall consent as hereinafter provided being hereinafter referred to as the Property's "PRIMARY INTENDED USE"). Tenant shall not use the Property for any other use without the prior written consent of Landlord, provided that Landlord shall not unreasonably withhold consent to any other laboratory, medical office and healthcare use permitted by Applicable Law and which shall not adversely affect the value of the Property as determined by a Qualified Appraiser. No use shall be made or permitted to be made of the Property and no acts shall be done thereon which will cause the cancellation of any insurance policy covering the Property, nor shall Tenant permit to be kept or used any article which

may be prohibited by law or by the standard form of fire insurance policies, or any other insurance policies required to be carried hereunder, or fire underwriter's regulations. Tenant shall, at its sole cost, comply with all of the requirements pertaining to the Property of any insurance board, association, organization or company necessary for the maintenance of insurance, as herein provided, covering the Property and Tenant's Personal Property, including, without limitation, the Insurance Requirements. Tenant shall not take or omit to take any action, the taking or omission of which may materially impair the value or the usefulness of the Property or any part thereof for the Primary Intended Use.

4.1.2 NECESSARY APPROVALS. Tenant shall proceed with all due diligence and exercise best efforts to obtain and maintain all approvals necessary to use and operate the Property for the Primary Intended Use.

4.1.3 LAWFUL USE, ETC. Tenant shall not use or suffer or permit the use of the Property or Tenant's Personal Property for any unlawful purpose. Tenant shall not commit or suffer to be committed any waste on the Property, nor shall Tenant cause or permit any nuisance thereon or therein. Tenant shall neither suffer nor permit the Property or any portion thereof, including any Capital Addition, or Tenant's Personal Property, to be used in such a manner as (a) might reasonably tend to impair Landlord's (or Tenant's, as the case may be) title thereto or to any portion thereof, or (b) may reasonably make possible a claim or claims for adverse usage or adverse possession by the public, as such, or of implied dedication of the Property or any portion thereof.

4.2 COMPLIANCE WITH LEGAL AND INSURANCE REQUIREMENTS, ETC. Subject to the provisions of ARTICLE 8, Tenant, at its sole expense, shall (a) comply with Legal Requirements and Insurance Requirements in respect of the use, operation, maintenance, repair, alteration and restoration of all of the Property, and (b) procure, maintain and comply with all appropriate licenses, permits, and other authorizations and agreements required for any use of the Property and Tenant's Personal Property then being made, and for the proper erection, installation, operation and maintenance of the Property or any part thereof, including, without limitation, any Capital Additions.

4.3 ENVIRONMENTAL MATTERS.

4.3.1 RESTRICTION ON USE, ETC. Tenant shall not store, spill upon, dispose of or transfer to or from the Property any Hazardous Substance, except that Tenant may store, transfer and dispose of Hazardous Substances in compliance with Applicable Laws. Tenant shall maintain the Property at all times free of any Hazardous Substance (except such Hazardous Substances as are maintained in compliance with all Applicable Laws). Tenant shall promptly: (a) at Landlord's request notify Landlord in writing of any change in the nature or extent of Hazardous Substances at the Property; (b) at Landlord=s request transmit to Landlord a copy of any Community Right to Know report which is required to be filed by Tenant with respect to the Property pursuant to SARA Title III or any other Applicable Law; (c) transmit to Landlord copies of any citations, orders, notices of responsibility or other governmental communications received by Tenant or its agents or representatives with respect to Hazardous Materials (collectively, "ENVIRONMENTAL NOTICE"), and copies of any reports or other information detailing any Hazardous Substance on the Property, which identify or could give rise to a violation of any Applicable Law and/or could give rise to any cost, expense, loss or damage exceeding $50,000 (an "ENVIRONMENTAL OBLIGATION"); (d) observe and comply with all Applicable Laws relating to the use, maintenance and disposal of Hazardous Substances and all orders or directives from any official, court or agency of competent jurisdiction relating to the use or maintenance or requiring the removal, treatment, containment or other disposition thereof; and (e) pay or otherwise dispose of any fine, charge or Imposition related thereto, unless Tenant shall contest the same in good faith and by appropriate proceedings and the right to use and the value of the Property is not materially and adversely affected thereby.

If, at any time prior to the termination of this Agreement, Hazardous Substances are discovered on the Property in violation of Applicable Law, Tenant shall take all actions and incur any and all expenses, as may be reasonably necessary and as may be required by any Government Agency, (i) to clean up and remove from and about the Property all Hazardous Substances thereon, (ii) to contain and prevent any further release or threat of release of Hazardous Substances on or about the Property and (iii) to eliminate any further release or threat of release of Hazardous Substances on or about the Property.

4.3.2 ENVIRONMENTAL REPORT. Six (6) months prior to expiration of the Term, Tenant, at its sole cost and expense, shall designate a qualified environmental engineer, reasonably satisfactory to Landlord, which engineer shall conduct an environmental investigation of the Property and prepare an environmental site assessment report (the "ENVIRONMENTAL REPORT") with respect thereto. The scope of such Environmental Report shall include, without limitation, review of relevant records, interviews with persons knowledgeable about the Property and relevant governmental agencies, a site inspection of the Property and adjoining properties (Phase I) and shall otherwise be reasonably satisfactory in form and substance to Landlord. If such investigation, in the opinion of the performing engineer, indicates that any portion of the Property is not free from oil, asbestos, radon and other Hazardous Substances, such investigation shall also include a more detailed physical site inspection, appropriate testing, subsurface and otherwise, and review of historical records (Phase II) to demonstrate the compliance of such of the Property with Applicable Laws and the absence of Hazardous Substances.

All preliminary drafts and final versions of the Environmental Report, and supplements and amendments thereto, shall be provided to Landlord contemporaneously with delivery thereof to Tenant. With respect to any recommendations contained in the Environmental Report, violations of Applicable Laws and/or the existence of any conditions at the Property which could give rise to an Environmental Obligation, Tenant shall promptly give Notice thereof to Landlord, together with a description, setting forth in reasonable detail, of all actions Tenant proposes to take in connection therewith and Tenant shall promptly take all actions, and incur any and all expenses, as may be reasonably necessary and as may be required by any Government Agency and as may be reasonably required by Landlord, (i) to clean up, remove or remediate from and about the Property all Hazardous Substances thereon, (ii) to contain, prevent and eliminate any further release or threat of release of Hazardous Substances on or about the Property, and (iii) otherwise to eliminate such violation or condition from the Property to the reasonable satisfaction of Landlord.

4.3.3 INDEMNIFICATION OF LANDLORD. Tenant shall protect, indemnify and hold harmless Landlord and each Facility Mortgagee, their trustees, officers, agents, employees and beneficiaries, and any of their respective successors or assigns (hereafter the "INDEMNITEES," and when referred to singly, an "INDEMNITEE") for, from and against any and all debts, liens, claims, causes of action, administrative orders or notices, costs, fines, penalties or expenses (including, without limitation, reasonable attorneys' fees and expenses) imposed upon, incurred by or asserted against any Indemnitee resulting from, either directly or indirectly, the presence in, upon or under the soil or ground water of any portion of the Property or (if caused by activity at the Property) any properties surrounding the Property of any Hazardous Substances in violation of any Applicable Law by reason of any failure by Tenant or any Person to perform or comply with any of the terms of this SECTION 4.3. Tenant's duty herein includes, but is not limited to, costs associated with personal injury or property damage claims as a result of the presence of Hazardous Substances in, upon or under the soil or ground water of any portion of the Property in violation of any Applicable Law but does not include any attribution of Landlord=s internal administrative costs. Upon Notice from Landlord, Tenant shall undertake the defense, at Tenant's sole cost and expense, of any indemnification duties set forth herein.

Tenant shall, upon demand, pay to Landlord, as Additional Rent, any cost, expense, loss or damage (including, without limitation, reasonable attorneys' fees) incurred by Landlord and arising from a failure of Tenant strictly to observe and perform the foregoing requirements, which amounts

shall bear interest five (5) days after the date of such demand until paid by Tenant to Landlord at the Overdue Rate.

Notwithstanding any of the foregoing to the contrary, in no event shall Tenant be required to indemnify Landlord against any damage arising from the negligence or other wrongful conduct of Landlord or its employees; nor be required to pay any settlement not approved by Tenant unless Tenant shall have failed to comply with its obligations under the first paragraph of this SECTION 4.3.3.

4.3.4 SURVIVAL. The provisions of this SECTION 4.3 shall survive the expiration or sooner termination of this Agreement.

ARTICLE 5
MAINTENANCE AND REPAIRS, ETC.

5.1 MAINTENANCE AND REPAIR.

5.1.1 TENANT'S OBLIGATIONS. Tenant shall, at its sole cost and expense, keep the Property and all private roadways, sidewalks and curbs appurtenant thereto (and Tenant's Personal Property) in good order and repair, reasonable wear and tear excepted (whether or not the need for such repairs occurs as a result of Tenant's use, any prior use, the elements or the passage of time), and shall promptly make all necessary and appropriate repairs and replacements thereto of every kind and nature, whether interior or exterior, structural or nonstructural, ordinary or extraordinary, foreseen or unforeseen or arising by reason of a condition existing prior to the commencement of the Term (concealed or otherwise); PROVIDED, HOWEVER, that Tenant shall be permitted to prosecute claims against Landlord's predecessors in title, as well as contractors and suppliers for breach of any representation or warranty made to or on behalf of Landlord, or for any latent defects in the Property. All repairs shall be made in good, workmanlike and first-class manner, in accordance with all applicable federal, state and local statutes, ordinances, by-laws, codes, rules and regulations relating to any such work. Tenant shall not take or omit to take any action, the taking or omission of which would materially impair the value of the Property or any part thereof for its Primary Intended Use. Tenant's obligations under this SECTION 5.1.1 shall be limited in the event of any casualty or Condemnation as set forth in SECTIONS 10.2 AND 11.2. Notwithstanding any provisions of this SECTION 5.1 to the contrary, Tenant's obligations with respect to Hazardous Substances are as set forth in SECTION 4.3.

Notwithstanding the foregoing, in the event that Landlord shall give notice to Tenant that Tenant is in default of its obligations under SECTION 5.1.1, such default shall not have arisen due to a casualty or a taking, or the requirements of Applicable Laws, and the cost of remedying such default shall exceed $1,000,000 (which amount shall be increased over the term of this Agreement by the increase in the Index from the Commencement Date to the date of such notice), then Landlord shall (at its sole discretion) either agree to provide to Tenant the funds necessary to cure such default, or excuse Tenant from curing such default. If Landlord shall agree to provide such funds then the Minimum Rent, as of the date(s) Landlord shall disburse the same, shall increase by one-twelfth of the product of (a) the amount of funds advanced multiplied by (b) the greater of (i) ten percent (10%) or (ii) the sum of the quoted per annum rate for fifteen year U.S. Treasury obligations on the date(s) of funding plus three hundred fifty (350) basis points; and the funds shall be disbursed upon receipt by Landlord of (i) lien waivers from all contractors performing the work for which such funds are provided, and (ii) evidence satisfactory to Landlord that all such work shall have been performed in a first-class manner and in compliance with Applicable Laws.

"INDEX" shall mean the Consumer Price Index for Urban Consumers, Boston-Lawrence-Salem, Massachusetts/New Hampshire, All Items, 1982-1984=100, (or the Consumer Price Index for the smallest geographic area for which includes Boston-Lawrence-Salem, Massachusetts/New Hampshire. The Index is presently published by the Bureau of Labor Statistics of the United States Department of

Labor. In the event publication of the Index ceases, then the Index shall be whatever index is published by the United States Department of Labor at that time that is most nearly comparable as a measure of general changes in price levels for such area.

5.1.2 LANDLORD'S OBLIGATIONS. Landlord shall not, under any circumstances, be required to build or rebuild any improvement on the Property, or to make any repairs, replacements, alterations, restorations or renewals of any nature or description to the Property, whether ordinary or extraordinary, structural or nonstructural, foreseen or unforeseen, or to make any expenditure whatsoever with respect thereto (except as provided in ARTICLES 10 AND 11 with respect to disbursement of insurance and Award proceeds), or to maintain the Property in any way, except as specifically provided herein. Tenant hereby waives, to the maximum extent permitted by law, the right to make repairs at the expense of Landlord pursuant to any law in effect on the date hereof or hereafter enacted. Landlord shall have the right to give, record and post, as appropriate, notices of nonresponsibility under any mechanic's lien laws now or hereafter existing.

5.1.3 NONRESPONSIBILITY OF LANDLORD; NO MECHANICS LIENS. Landlord's interest in the Property shall not be subject to liens for Capital Additions made by Tenant and Tenant shall have no power or authority to create any lien or permit any lien to attach to any of the Property or the present estate, reversion or other estate of Landlord in the Property or on the building or other improvements thereon as a result of Capital Additions made by Tenant or for any other cause or reason. All materialmen, contractors, artisans, mechanics and laborers and other persons contracting with Tenant with respect to the Property, or any part thereof, are hereby charged with notice that such liens are expressly prohibited and that they must look solely to Tenant to secure payment for any work done or material furnished for Capital Additions by Tenant or for any other purpose during the term of this Agreement.

Nothing contained in this Agreement shall be deemed or construed in any way as constituting the consent or request of Landlord, express or implied, by inference or otherwise, to any contractor, subcontractor, laborer or materialmen for the performance of any labor or the furnishing of any materials for any alteration, addition, improvement or repair to the Property or any part thereof or as giving Tenant any right, power or authority to contract for or permit the rendering of any services or the furnishing of any materials that would give rise to the filing of any lien against the Property or any part thereof nor to subject Landlord's estate in the Property or any part thereof to liability under any mechanic's or materialmen's lien Law of the State in any way, it being expressly understood Landlord's estate shall not be subject to any such liability.

5.2 TENANT'S PERSONAL PROPERTY. Tenant may, at its expense, install, affix or assemble or place on any parcels of the Land, any items of Tenant's Personal Property; and Tenant may, subject to the conditions set forth below, remove the same at any time, provided that no Default or Event of Default has occurred and is continuing. Tenant shall provide and maintain throughout the Term all such Tenant's Personal Property as shall be necessary in order to operate the Facility, in compliance with applicable Legal Requirements and Insurance Requirements. All of Tenant's Personal Property not removed by Tenant on or prior to the expiration or earlier termination of this Agreement shall be considered abandoned by Tenant and may be appropriated, sold, destroyed or otherwise disposed of by Landlord without the necessity of first giving notice thereof to Tenant, without any payment to Tenant and without any obligation to account therefor. Tenant shall, at its expense, restore the Property to the condition required by SECTION 5.3, including repair of all damage to the Property caused by the removal of Tenant's Personal Property, whether effected by Tenant or Landlord.

5.3 YIELD UP. Upon the expiration or sooner termination of this Agreement, Tenant shall vacate and surrender the Property to Landlord free from Tenant's Personal Property and free from any Hazardous Substances and in the condition in which the Property was in on the Commencement Date, except as repaired, rebuilt, restored, altered or added to as permitted or required by the provisions of this

Agreement, reasonable wear and tear (and casualty damage and Condemnation, in the event that this Agreement is terminated following a casualty or total Condemnation in accordance with ARTICLE 10 or ARTICLE 11) excepted. Notwithstanding the foregoing, Tenant shall not be required to remove fixtures which, at the expiration or sooner termination of this Agreement, shall be in compliance with Applicable Law and remain in good order and condition, nor shall Tenant be required to remove Hazardous Materials which were either part of the Facility base building construction at the Commencement Date or which are added to the Facility during the term with Landlord=s consent, but without conditioning of such consent on removal by Tenant, and in either case which, at the expiration or sooner termination of this Agreement, shall be in compliance with Applicable Laws.

5.4 ENCROACHMENTS, RESTRICTIONS, ETC. If any of the Improvements shall, at any time, encroach upon any property, street or right-of-way adjacent to the Property, or shall violate the agreements or conditions contained in any lawful restrictive covenant or other agreement affecting the Property, or any part thereof, or shall impair the rights of others under any easement or right-of-way to which the Property is subject, upon the request of Landlord (but only as to any encroachment, violation or impairment that is not a Permitted Encumbrance) or of any Person affected by any such encroachment, violation or impairment, Tenant shall, at its sole cost and expense, subject to its right to contest the existence of any encroachment, violation or impairment in accordance with the provisions of ARTICLE 8, either (a) obtain valid and effective waivers or settlements of all claims, liabilities and damages resulting from each such encroachment, violation or impairment, whether the same shall affect Landlord or Tenant, or (b) make such changes in the Leased Improvements and take such other actions, as are necessary to remove such encroachment and to end such violation or impairment, including, if necessary, the alteration of any of the Improvements and, in any event, take all such actions as may be necessary in order to ensure the continued operation of the Facility for the Primary Intended Use substantially in the manner and to the extent such Facility was operated prior to the assertion of such violation, impairment or encroachment. Any such alteration shall be made in conformity with the applicable requirements of this ARTICLE 5. Tenant's obligations under this SECTION 5.4 shall be in addition to and shall in no way discharge or diminish any obligation of any insurer under any policy of title or other insurance.

5.5 LANDLORD TO GRANT EASEMENTS, ETC. Landlord shall from time to time, so long as no Default or Event of Default shall have occurred and be continuing, at the request of Tenant and at Tenant's sole cost and expense, (a) grant easements and other rights in the nature of easements with respect to the Property to third parties; (b) release existing easements or other rights in the nature of easements which are for the benefit of the Property; (c) dedicate or transfer unimproved portions of the Property for road, highway or other public purposes; (d) execute petitions to have the Property annexed to any municipal corporation or utility district; (e) execute amendments to any covenants and restrictions affecting the Property; and (f) execute and deliver to any Person any instrument appropriate to confirm or effect such grants, release, dedications, transfers, petitions and amendments (to the extent of its interests in the Property); PROVIDED, HOWEVER, that Landlord shall have first determined that such grant, release, dedication, transfer, petition or amendment is not detrimental to the operation of the Property for the Primary Intended Use and does not materially reduce the value of the Property, and Landlord shall have received an Officer's Certificate confirming such determination, together with such additional ainformation with respect thereto as Landlord may reasonably request.

ARTICLE 6
CAPITAL ADDITIONS, ETC.

6.1 CONSTRUCTION OF CAPITAL ADDITIONS. Tenant shall not construct or install Capital Additions on the Property without obtaining Landlord's prior written consent, provided that no consent shall be required for any Capital Addition so long as (a) the Capital Additions Costs for such Capital Addition are less than $150,000 in the aggregate; (b) such construction or installation would not adversely affect or violate any Legal Requirement or Insurance Requirement applicable to the Property; (c) the Capital Addition Costs incurred or to be incurred by Tenant in the twelve-month period ending with the completion of the latest Capital Additions shall not exceed $500,000; and (d) Landlord shall have received an Officer's Certificate certifying as to the satisfaction of the conditions set out in clauses (a), (b) and (c) above. Landlord shall not unreasonably withhold consent to any Capital Addition which shall not alter the character of the Property or diminish the value of the Property (which, in the event of a dispute, shall be determined by a Qualified Appraiser selected by Landlord and reasonably acceptable to Tenant). If Landlord's consent is required, prior to commencing construction of any Capital Addition, Tenant shall submit to Landlord, in writing, a proposal setting forth, in reasonable detail, any proposed Capital Addition and, if required by Landlord, the report of the Qualified Appraiser attesting to effect on value and shall provide to Landlord such plans and specifications, permits, licenses, contracts and other information concerning the proposed Capital Addition as Landlord may reasonably request. Landlord shall have thirty (30) days to review all materials submitted to Landlord in connection with any such proposal. Failure of Landlord to respond to Tenant's proposal within thirty (30) days after receipt of all information and materials requested by Landlord in connection with the proposed Capital Addition shall be deemed to constitute approval of such proposed Capital Addition, provided that such proposal states prominently that the failure of Landlord to respond within such 30-day period shall constitute approval. Without limiting the generality of the foregoing, such proposal shall indicate the approximate projected cost of constructing such Capital Addition and the use or uses to which it will be put. No Capital Addition shall be made which would tie in or connect any Improvement on the Property with any other improvements on property adjacent to the Property. Any Capital Additions shall, upon the expiration or sooner termination of this Agreement, pass to and become the property of Landlord, free and clear of all encumbrances other than Permitted Encumbrances.

6.2 NON-CAPITAL ADDITIONS. Tenant shall have the right, at Tenant's sole cost and expense, without Landlord consent, to make additions, modifications or improvements to the Property which are not Capital Additions ("NON-CAPITAL ADDITIONS") from time to time as Tenant, in its discretion, may deem desirable for the Primary Intended Use (including, without limitation, the improvement, in a fashion consistent with the remainder of the Facility, of portions of the Facility that are, as of the Commencement Date, unfinished shelf space) provided that any such Non-Capital Addition will not materially alter the character or purpose or materially detract from the value or operating efficiency of the Property or adversely affect the ability of Tenant to comply with the provisions of this Agreement and, without limiting the foregoing, will not adversely affect or violate any Legal Requirement or Insurance Requirement applicable to the Property. All such Non-Capital Additions shall, upon expiration or earlier termination of this Agreement, pass to and become the property of Landlord, free and clear of all liens and encumbrances, other than Permitted Encumbrances.

ARTICLE 7
LIENS

Subject to ARTICLE 8, Tenant shall not, directly or indirectly, create or allow to remain and shall promptly discharge or bond over in a manner reasonably satisfactory to Landlord, at its expense, any lien, encumbrance, attachment, title retention agreement or claim upon the Property or Tenant's leasehold interest therein or any attachment, levy, claim or encumbrance in respect of the Rent, other than (a) Permitted Encumbrances; (b) restrictions, liens and other encumbrances which are consented to in

writing by Landlord (which shall, upon such consent, become "Permitted Encumbrances"); (c) liens for those taxes of Landlord which Tenant is not required to pay hereunder; (d) subleases permitted by ARTICLE 17; (e) liens for Impositions or for sums resulting from noncompliance with Legal Requirements so long as (i) the same are not yet payable, or (ii) are being contested in accordance with ARTICLE 8; (f) liens of mechanics, laborers, materialmen, suppliers or vendors incurred in the ordinary course of business that are not yet due and payable or are for sums that are being contested in accordance with ARTICLE 8; and (g) any Facility Mortgages or other liens which are the responsibility of Landlord pursuant to the provisions of ARTICLE 21.

ARTICLE 8
PERMITTED CONTESTS

Tenant shall have the right to contest the amount or validity of any Imposition, Legal Requirement, Insurance Requirement, lien, attachment, levy, encumbrance, charge or claim (collectively, "CLAIMS") by appropriate legal proceedings, conducted in good faith and with due diligence, provided that (a) the foregoing shall in no way be construed as relieving, modifying or extending Tenant's obligation to pay any Claims as finally determined; (b) such contest shall not cause Tenant to be in default under any mortgage or deed of trust encumbering its interest in the Property or result in a lien attaching to the Property which is not discharged or bonded within 10 days of Notice to Tenant of its attachment; (c) no part of the Property nor any Rent therefrom shall be in any immediate danger of sale, forfeiture, attachment or loss; and (d) Tenant shall indemnify and hold harmless Landlord from and against any cost, claim, damage, penalty or reasonable expense, including reasonable attorneys' fees, incurred by Landlord in connection therewith or as a result thereof. Upon Landlord's request, which request may be made by Landlord only if the Security Deposit then held by Landlord shall not be at least three times the amount of the Claim (together with interest and penalties), Tenant shall either (i) provide a bond, title indemnity, endorsement or other assurance reasonably satisfactory to Landlord that all Claims which may be assessed against the Property, together with all interest and penalties thereon will be paid, or (ii) deposit within the time otherwise required for payment with a bank or trust company, as trustee, as security for the payment of such Claims, an amount sufficient to pay the same, together with interest and penalties in connection therewith and all Claims which may be assessed against or become a Claim on the Property, or any part thereof, in connection with any such contest. Tenant shall furnish Landlord and any Facility Mortgagee with reasonable evidence of such deposit, title indemnity, endorsement or other assurance within five (5) days after request therefor. Landlord agrees to join in any such proceedings if required legally to prosecute such contest, provided that Landlord shall not thereby be subjected to any liability therefor (including, without limitation, for the payment of any costs or expenses in connection therewith). Tenant shall be entitled to any refund of any Claims and such charges and penalties or interest thereon which have been paid by Tenant or paid by Landlord and for which Landlord has been fully reimbursed by Tenant. If Tenant shall fail (x) to pay any Claims when finally determined, (y) to provide security therefor as provided in this ARTICLE 8, or (z) to prosecute any such contest diligently and in good faith, Landlord may, upon reasonable notice to Tenant which notice shall not be required if Landlord shall reasonably determine that the same is not practicable), pay such charges, together with interest and penalties due with respect thereto, and Tenant shall reimburse Landlord therefor, upon demand, as Additional Rent.

ARTICLE 9
INSURANCE AND INDEMNIFICATION

9.1 GENERAL INSURANCE REQUIREMENTS. Tenant shall, at all times during the Term and at any other time Tenant shall be in possession of the Property, keep the Property and all property located therein or thereon, including Tenant's Personal Property, insured against the risks and in the amounts as follows and shall maintain the following insurance:

(a) "All-risk" property insurance, including insurance against loss or damage by fire, vandalism and malicious mischief, explosion of steamboilers, pressure vessels or other similar apparatus, now or hereafter installed in the Facility, extended coverage perils, earthquake and all physical loss perils insurance, including, but not limited to, sprinkler leakage, in an amount equal to one hundred percent (100%) of the then full Replacement Cost thereof (as defined in SECTION 9.2) with the usual extended coverage endorsements, including a Replacement Cost and Agreed Amount Endorsement and Builder's Risk Coverage during the continuance of any construction at the Property;

(b) Loss of rents insurance in an amount not less than the Rent due for any succeeding twenty-four (24) month period hereunder;

(c) Commercial general liability insurance, including bodily injury and property damage (on an occurrence basis and on a 1988 ISO CGL form or its equivalent or otherwise in the broadest form available, including, without limitation, broad form contractual liability, fire legal liability, independent contractor's hazard and completed operations coverage) in an amount not less than One Million Dollars ($1,000,000) per occurrence, Two Million Dollars ($2,000,000) in the aggregate and umbrella coverage of all such claims in an amount not less than Twenty Million Dollars ($20,000,000);

(d) Flood (if the Property is located in whole or in part within an area identified as an area having special flood hazards and in which flood insurance has been made available under the National Flood Insurance Act of 1968, as amended, or the Flood Disaster Protection Act of 1973, as amended (or any successor acts thereto)) and such other hazards and in such amounts as may be customary for comparable properties in the area;

(e) Worker's compensation insurance coverage for all persons employed by Tenant on the Property with statutory limits and otherwise with limits of and provisions in accordance with the requirements of applicable local, State and federal law, and employer's liability insurance in such amounts as Landlord shall reasonably require; and

(f) Such additional insurance or increased limits on the coverages stated above as may be reasonably required, from time to time, by Landlord or any Facility Mortgagee.

9.2 REPLACEMENT COST. "REPLACEMENT COST" as used herein shall mean the actual replacement cost of the property requiring replacement from time to time, including an increased cost of construction endorsement, less exclusions provided in the standard form of fire insurance policy. In the event either party believes that the then full Replacement Cost has increased or decreased at any time during the Term, such party, at its own cost, shall have the right to have such full Replacement Cost redetermined by an accredited appraiser approved by the other, which approval shall not be unreasonably withheld or delayed. The party desiring to have the full Replacement Cost so redetermined shall forthwith, on receipt of such determination by such appraiser, give written notice thereof to the other. The determination of such appraiser shall be final and binding on the parties hereto, and Tenant shall forthwith conform the amount of the insurance carried to the amount so determined by the appraiser.

9.3 WAIVER OF SUBROGATION. Landlord and Tenant agree that (insofar as and to the extent that such agreement may be effective without invalidating or making it impossible to secure insurance coverage from responsible insurance companies doing business in the State) with respect to any property loss which is covered by insurance then being carried by Landlord or Tenant, respectively, the party carrying such insurance and suffering said loss releases the other of and from any and all claims with respect to such loss; and they further agree that their respective insurance companies shall have no right of subrogation against the other on account thereof, even though extra premium may result therefrom. In the event that any extra premium is payable by Tenant as a result of this provision, Landlord shall not be liable for reimbursement to Tenant for such extra premium.

9.4 FORM SATISFACTORY, ETC. All insurance policies and endorsements required pursuant to this ARTICLE 9 shall be fully paid for, nonassessable and shall contain such provisions and expiration dates and be

in such form and amounts and issued by insurance carriers authorized to do business in the State, having a general policy holder's rating of A or A+ in Best's latest rating guide, and as otherwise shall be reasonably approved by Landlord. Without limiting the foregoing, such policies shall include no deductible in excess of $25,000 (unless consistent with deductibles included in policies carried by entities engaged in similar businesses and owning similar properties similarly situated and agreed to in advance by Landlord) and, with the exception of the insurance described in SECTION 9.1(E), shall name Landlord and any Facility Mortgagee as additional insureds, as their interests may appear except that the insurance under Section 9.1(a) and (b) above shall list Landlord as the first named insured. All losses shall be payable to Landlord, any Facility Mortgagee or Tenant as provided in ARTICLE 10. Any loss adjustment shall require the prior written consent of Landlord, Tenant, and each Facility Mortgagee. Tenant shall pay all insurance premiums and deliver policies or certificates thereof to Landlord prior to their effective date (and, with respect to any renewal policy, thirty (30) days prior to the expiration of the existing policy) and, in the event Tenant shall fail to effect such insurance as herein required, to pay the premiums therefor or to deliver such policies or certificates to Landlord or any Facility Mortgagee at the times required, Landlord shall have the right, but not the obligation, to acquire such insurance and pay the premiums therefor, which amounts shall be payable to Landlord, upon demand, as Additional Rent, together with interest accrued thereon at the Overdue Rate from the date such demand is made until the date repaid. All such policies shall provide Landlord (and any Facility Mortgagee, if required by the same) thirty (30) days' prior written notice of any modification, expiration or cancellation of such policy.

9.5 BLANKET POLICY. Notwithstanding anything to the contrary contained in this ARTICLE 9, Tenant's obligation to maintain the insurance herein required may be brought within the coverage of a so-called blanket policy or policies of insurance carried and maintained by Tenant and its Affiliated Persons, provided, that (a) the coverage thereby afforded will not be reduced or diminished from that which would exist under a separate policy meeting all other requirements of this Agreement, and (b) the requirements of this ARTICLE 9 are otherwise satisfied. Without limiting the foregoing, the amounts of insurance that are required to be maintained pursuant to Section 9.1 shall be on a Facility by Facility basis, and shall not be subject to an aggregate limit.

9.6 NO SEPARATE INSURANCE. Tenant shall not take out separate insurance, concurrent in form or contributing in the event of loss with that required by this ARTICLE 9, or increase the amount of any existing insurance by securing an additional policy or additional policies, unless all parties having an insurable interest in the subject matter of such insurance, including Landlord and all Facility Mortgagees, are included therein as additional insureds and the loss is payable under such insurance in the same manner as losses are payable under this Agreement. In the event Tenant shall take out any such separate insurance or increase any of the amounts of the then existing insurance, Tenant shall give Landlord prompt Notice thereof.

9.7 INDEMNIFICATION OF LANDLORD. Notwithstanding the existence of any insurance provided for herein and without regard to the policy limits of any such insurance, Tenant shall protect, indemnify and hold harmless Landlord for, from and against all liabilities, obligations, claims, damages, penalties, causes of action, costs and reasonable expenses (including, without limitation, reasonable attorneys' fees), to the maximum extent permitted by law, imposed upon or incurred by or asserted against Landlord by reason of: (a) any accident, injury to or death of persons or loss of or damage to property occurring on or about the Property or adjoining sidewalks or rights of way, including, without limitation, any claims of malpractice; (b) any past, present or future use, misuse, non-use, condition, management, maintenance or repair by Tenant or anyone claiming under Tenant of the Property or Tenant's Personal Property or any litigation, proceeding or claim by governmental entities or other third parties to which Landlord is made a party or participant relating to the Property and arising during the Term or Tenant's Personal Property or such use, misuse, non-use, condition, management, maintenance, or repair thereof including, failure to perform obligations (other than Condemnation proceedings) to which Landlord is made a party; (c) any Impositions (which are the obligations of Tenant to pay pursuant to the applicable provisions of this Agreement);

and (d) any failure on the part of Tenant or anyone claiming under Tenant to perform or comply with any of the terms of this Agreement. Subject to the provisions of Article 8, Tenant shall pay all amounts payable under this SECTION 9.7 within ten (10) days after demand therefor, and if not timely paid, such amounts shall bear interest at the Overdue Rate from the date due to the date of payment. Tenant, at its expense, shall contest, resist and defend any such claim, action or proceeding asserted or instituted against Landlord or may compromise or otherwise dispose of the same, provided Landlord shall be fully released or bonded off in form satisfactory to Landlord. The obligations of Tenant under this SECTION 9.7 are in addition to the obligations set forth in SECTION 4.4 and shall survive the termination of this Agreement.

ARTICLE 10
CASUALTY

10.1 INSURANCE PROCEEDS. All proceeds payable by reason of any loss or damage to the Property, or any portion thereof, and insured under any policy of insurance required by ARTICLE 9 (including, without limitation, proceeds of any loss of rents insurance) shall be paid directly to Landlord (subject to the provisions of SECTION 10.2). If Tenant is required to reconstruct or repair the Property as provided herein, such proceeds shall be paid out by Landlord from time to time for the reasonable costs of reconstruction or repair of the Property necessitated by such damage or destruction, subject to the provisions of SECTION 10.2.4. Any excess proceeds of insurance remaining after the completion of the restoration shall be paid to Tenant, except for any portion reasonably reserved against any Event of Default that has occurred and is continuing. In the event that SECTION 10.2.1 below is applicable, the insurance proceeds shall be retained by the party entitled thereto pursuant to SECTION 10.2.1. All salvage resulting from any risk covered by insurance shall belong to Landlord, except that any salvage related to Tenant's Capital Additions and Tenant's Personal Property shall belong to Tenant and Landlord shall apply the proceeds received for any salvage to the costs paid by Tenant for restoration.

10.2 DAMAGE OR DESTRUCTION.

10.2.1 DAMAGE OR DESTRUCTION OF LEASED PROPERTY. If, during the Term, the Property shall be totally or partially destroyed and the Facility located thereon is thereby rendered Unsuitable for Its Primary Intended Use, Tenant shall purchase the Property from Landlord for a purchase price equal to the Adjusted Purchase Price of the Property. If Tenant purchases the Property as provided herein, the closing with respect thereto shall occur on a date designated by Landlord by Notice to Tenant (but in no event prior to 30 days after such Notice), this Agreement shall terminate upon payment of the purchase price therefor, and Landlord shall remit to Tenant all insurance proceeds pertaining to the Property then held by Landlord and shall assign to Tenant all rights to any proceeds available to Landlord under the insurance policies carried by Tenant pursuant to Section 9.1(a).

10.2.2 PARTIAL DAMAGE OR DESTRUCTION. If, during the Term, the Property shall be totally or partially destroyed but the Facility located thereon is not rendered Unsuitable for Its Primary Intended Use, Tenant shall promptly restore such Facility as provided in SECTION 10.2.4.

10.2.3 INSUFFICIENT INSURANCE PROCEEDS. If the cost of the repair or restoration of the Property exceeds the amount of insurance proceeds received by Landlord pursuant to ARTICLE 9, Tenant shall contribute any excess amounts needed to restore the Property. Such difference shall be paid by Tenant to Landlord and held by Landlord, together with any other insurance proceeds, for application to the cost of repair and restoration.

10.2.4 DISBURSEMENT OF PROCEEDS. In the event Tenant is required to restore the Property pursuant to SECTION 10.2, Tenant shall, at its sole cost and expense, commence promptly and continue diligently to perform the repair and restoration of the Property (hereinafter called the "WORK"), or shall cause the same to be done, so as to restore it in full compliance with all Legal Requirements so that the Property shall be at least equal in value and general utility to its general utility and value

immediately prior to such damage or destruction and substantially similar thereto. Subject to the terms hereof, Landlord shall advance the casualty insurance proceeds available under the policy carried by Tenant pursuant to Section 9.1(a) and the amounts paid to Landlord pursuant to SECTION 10.2.3 to Tenant regularly during the repair and restoration period so as to permit payment for the cost of any such restoration and repair. Any such advances shall be for not less than $25,000 (or such lesser amount as equals the entire balance of the repair and restoration) and Tenant shall submit to Landlord a written requisition and substantiation therefor on AIA Forms G702 and G703 (or on such other form or forms as may be reasonably acceptable to Landlord). Landlord may, at its option, condition advancement of said insurance proceeds and other amounts on (a) the absence of any Event of Default; (b) its reasonable approval of plans and specifications of an architect reasonably satisfactory to Landlord; (c) general contractors' estimates; (d) architect's certificates; (e) unconditional lien waivers of general contractors; (f) evidence of approval by all governmental authorities and other regulatory bodies whose approval is required; and (g) such other certificates as Landlord may, from time to time, reasonably require. Proceeds of loss of rents insurance shall be applied by Landlord, on the first day of the calendar month following such disbursement, first to the payment of all Minimum Rent, Additional Rent and Additional Charges then due and payable and to become due and payable for the period for which such proceeds have been paid by the insurance provider, and the balance, if any, to Tenant. If, at any time, the amount of such proceeds will be insufficient to pay all Minimum Rent, Additional Rent and Additional Charges due or to come due during such period, Landlord may, in its sole discretion, suspend disbursement of any casualty proceeds to Tenant.

10.3 DAMAGE NEAR END OF TERM. Notwithstanding any provisions of SECTION 10.1 OR 10.2 to the contrary, if damage to or destruction of the Property occurs during the last twenty-four (24) months of the Term and if such damage or destruction cannot reasonably be expected to be fully repaired and restored prior to the date that is six (6) months prior to the end of such Term, the provisions of SECTION 10.2.1 shall apply as if the Property had been totally or partially destroyed and the Facility located thereon rendered Unsuitable for its Primary Intended Use.

10.4 TENANT'S PROPERTY. All insurance proceeds payable by reason of any loss of or damage to any of Tenant's Personal Property or Tenant's Capital Additions shall be paid to Tenant and, to the extent necessary to repair or replace Tenant's Capital Additions or Tenant's Personal Property in accordance with SECTION 10.5, Tenant shall apply such proceeds only toward the cost of repairing or replacing damaged Tenant's Personal Property or Tenant's Capital Additions.

10.5 RESTORATION OF TENANT'S PROPERTY. If Tenant is required to restore the Property as hereinabove provided, Tenant shall either (a) restore those items of Tenant's Personal Property needed for the efficient operation of the Facility, or (b) replace such items with items of the same or better quality and utility.

10.6 NO ABATEMENT OF RENT. This Agreement shall remain in full force and effect and Tenant's obligation to make all payments of Rent and to pay all other charges as and when required under this Agreement shall, except as otherwise provided in SECTION 10.2.1, remain unabated during the Term notwithstanding any damage involving the Property (provided that Landlord shall credit against such payments any amounts paid to Landlord as a consequence of such damage under any business interruption insurance obtained by Tenant hereunder). The provisions of this ARTICLE 10 shall be considered an express agreement governing any cause of damage or destruction to the Property and, to the maximum extent permitted by Applicable Law, no local or State statute, law, rule, regulation or ordinance in effect during the Term which provide for such a contingency shall have any application in such case.

10.7 WAIVER. Tenant hereby waives any statutory rights of termination which may arise by reason of any damage or destruction of the Property.

ARTICLE 11
CONDEMNATION

11.1 TOTAL CONDEMNATION, ETC. If either (a) the whole of the Property shall be taken by Condemnation or (b) a Condemnation of less than the whole of the Property renders the Property Unsuitable for Its Primary Intended Use, this Agreement shall terminate as of the date of such condemnation, and Tenant and Landlord shall seek the Award for their interests in the Property as provided in SECTION 11.5. If the Award received by Landlord for Landlord's interest in the Property is less than the Adjusted Purchase Price, Tenant shall contribute and pay to Landlord the amount of such shortfall.

11.2 PARTIAL CONDEMNATION. In the event of a Condemnation of less than the whole of the Property such that the Property is still suitable for its Primary Intended Use, Tenant shall, at its sole cost and expense, commence promptly and continue diligently to restore the untaken portion of the Improvements on the Property so that such Improvements shall constitute a complete architectural unit of the same general character and condition (as nearly as may be possible under the circumstances) as the Improvements existing immediately prior to such Condemnation, in full compliance with all Legal Requirements. Subject to the terms hereof, Landlord shall contribute to the cost of restoration that part of the Award necessary to complete such repair or restoration, together with severance and other damages awarded for the taken Improvements, to Tenant regularly during the restoration period so as to permit payment for the cost of such repair or restoration. Landlord may, at its option, condition advancement of such Award and other amounts on (a) the absence of any Default or Event of Default; (b) its approval of plans and specifications of an architect satisfactory to Landlord (which approval shall not be unreasonably withheld or delayed); (c) general contractors' estimates; (d) architect's certificates; (e) unconditional lien waivers of general contractors; (f) evidence of approval by all governmental authorities and other regulatory bodies whose approval is required; and (g) such other certificates as Landlord may, from time to time, reasonably require. Landlord's obligation under this SECTION 11.2 to disburse the Award and such other amounts shall be subject to the collection thereof by Landlord. Tenant's obligation to restore the Property shall be subject to the release of the Award by the Facility Mortgagee to Landlord and Landlord=s release of the Award to Tenant in accordance with the terms of this Agreement. If the cost of the restoration of the Property exceeds that part of the Award necessary to complete such restoration, together with severance and other damages awarded for the taken Improvements, Tenant shall contribute upon the demand of Landlord any excess amounts needed to restore the Property. Such difference shall be paid by Tenant to Landlord and held by Landlord, together with such part of the Award and such severance and other damages, for application to the cost of restoration.

11.3 ABATEMENT OF RENT. Other than as specifically provided in this Agreement, this Agreement shall remain in full force and effect and Tenant's obligation to make all payments of Rent and to pay all other charges as and when required under this Agreement shall remain unabated during the Term notwithstanding any Condemnation. The provisions of this ARTICLE 11 shall be considered an express agreement governing any Condemnation and, to the maximum extent permitted bylaw, no local or State statute, law, rule, regulation or ordinance in effect during the Term which provides for such a contingency shall have any application in such case. Notwithstanding the foregoing, to the extent this Agreement shall not be terminated due to any Condemnation but Landlord shall receive an Award which it shall not remit to Tenant and which shall not be available to Tenant for restoration as provided in Section 11.2 (the "RETAINED AWARD") then the Minimum Rent due from time to time shall be reduced by the percentage determined by dividing the Retained Award by the Adjusted Purchase Price.

11.4 TEMPORARY CONDEMNATION. In the event of any temporary Condemnation of all or any part of the Property or Tenant's interest therein, this Agreement shall continue in full force and effect, and Tenant shall continue to pay, in the manner and on the terms herein specified, the full amount of the Rent. Tenant shall continue to perform and observe all of the other terms and conditions this Agreement on the part of the Tenant to be performed and observed. Provided no Default or Event of Default has occurred and is

continuing, the entire amount of any Award made for such temporary Condemnation allocable to the Term, whether paid by way of damages, rent or otherwise, shall be paid to Tenant. Tenant shall, promptly upon the termination of any such period of temporary Condemnation, at its sole cost and expense, restore the Property to the condition that existed immediately prior to such Condemnation, in full compliance with all Legal Requirements, unless such period of temporary Condemnation shall extend beyond the expiration of the Term, in which event Tenant shall not be required to make such restoration. For purposes of this SECTION 11.4, a Condemnation shall be deemed to be temporary if the period of such Condemnation is not expected to exceed twenty-four (24) months.

11.5 ALLOCATION OF AWARD. Except as provided in the second sentence of this SECTION 11.5, the total Award shall be solely the property of and payable to Landlord. Any portion of the Award made for the taking of Tenant's leasehold interest in the Property, Tenant's Capital Additions, loss of business during the remainder of the Term, the taking of Tenant's Personal Property, or Tenant's removal and relocation expenses shall be the sole property of and payable to Tenant (subject to the provisions of SECTION 11.2). In any Condemnation proceedings, Landlord and Tenant shall each seek its own Award in conformity herewith, at its own expense.

ARTICLE 12
DEFAULTS AND REMEDIES

12.1 EVENTS OF DEFAULT. The occurrence of any one or more of the following events shall constitute an "EVENT OF DEFAULT" hereunder:

(a) should Tenant fail to make any payment of Rent when due and such failure shall continue for a period of at least five (5) Business Days after Notice thereof; or

(b) should Tenant shall fail to maintain the insurance coverages required under ARTICLE 9 and such failure shall continue for a period of at least five (5) Business Days after Notice; or

(c) should Tenant default in the due observance or performance of any of the terms, covenants or agreements contained herein to be performed or observed by it (other than as specified in clauses (a) and (b) above) and such default shall continue for a period of thirty (30) days after Notice thereof from Landlord to Tenant (provided that Notice but no such cure period shall be required if Landlord shall reasonably determine immediate action is necessary to protect person or property); PROVIDED, HOWEVER, that if such default is susceptible of cure but such cure cannot be accomplished with due diligence within such period of time and if, in addition, Tenant commences to cure such default within thirty (30) days after Notice thereof from Landlord and thereafter prosecutes the curing of such default with all due diligence and Landlord shall not be materially affected by the continuing uncured default, such period of time shall be extended to such period of time (not to exceed an additional ninety (90) days in the aggregate) as may be necessary to cure such default with all due diligence; or

(d) should Tenant have failed to pay Rent timely at least three times during any twelve-month period during the Term and Landlord shall have given Tenant at least two (2) Notices during any such twelve-month period of Tenant's failure to pay Rent when due; or

(e) should there occur a final unappealable determination by applicable State authorities of the revocation or limitation of any license, permit, certification or approval required for the lawful operation of the Facility in accordance with the Primary Intended Use; or

(f) should any representation or warranty made by or on behalf of Tenant or any other Person under or in connection with this Agreement, or in any document, certificate or agreement delivered in connection herewith or therewith prove to have been false or misleading in any material respect on the date when made or deemed made; or

(g) should Tenant generally not be paying its debts as they become due, or should Tenant make a general assignment for the benefit of creditors; or

(h) should any petition be filed by or against Tenant under the Federal bankruptcy laws, or should any other proceeding be instituted by or against Tenant seeking to adjudicate it a bankrupt or insolvent, or seeking liquidation, reorganization, arrangement, adjustment or composition of it or its debts under any law relating to bankruptcy, insolvency or reorganization or relief of debtors, or seeking the entry of an order for relief or the appointment of a receiver, trustee, custodian or other similar official for Tenant, or for any substantial part of the property of Tenant, and such proceeding is not dismissed, stayed or bonded against within ninety (90) days after institution thereof, or should Tenant take any action to authorize or effect any of the actions set forth above in this paragraph; or

(i) should Tenant institute any proceeding for its dissolution or termination; or

(j) should Tenant voluntarily cease operation of the Property for the Primary Intended Use for a period in excess of thirty (30) consecutive days, except as a result of damage, destruction or partial or complete Condemnation; or

(k) should a default occur under any mortgage which is secured by Tenant's leasehold interest hereunder entitling the holder to accelerate the debt secured thereby or to commence foreclosure proceedings in connection with said mortgage; or

(l) should the estate or interest of Tenant in the Property or any part thereof be levied upon or attached in any proceeding and the same shall not be vacated or discharged within the later of (x) one hundred and twenty (120) days after commencement thereof, unless the amount in dispute is less than $100,000, in which case Tenant shall give Notice to Landlord of the dispute but Tenant may defend in any suitable way, and (y) thirty (30) days after receipt by Tenant of Notice thereof from Landlord (unless Tenant shall be contesting such lien or attachment in good faith in accordance with ARTICLE 8);

then, and in any such event, Landlord, in addition to all other remedies available to it, may terminate this Agreement by giving Notice thereof to Tenant and upon the expiration of the time, if any, fixed in such Notice, this Agreement shall terminate and all rights of Tenant under this Agreement shall cease. Landlord shall have and may exercise all rights and remedies available at law and in equity to Landlord as a result of Tenant's breach of this Agreement.

Upon the occurrence of an Event of Default, Landlord may, in addition to any other remedies provided herein, subject to Applicable Law, enter upon the Property or any portion thereof and take possession of any and all of Tenant's Personal Property on the Property without liability for trespass or conversion (Tenant hereby waiving any right to notice or hearing prior to such taking of possession by Landlord) and sell the same at public or private sale, after giving Tenant reasonable Notice of the time and place of any public or private sale, at which sale Landlord or its assigns may purchase all or any portion of Tenant's Personal Property unless otherwise prohibited by law. Unless otherwise provided by law and without intending to exclude any other manner of giving Tenant reasonable notice, the requirement of reasonable Notice shall be met if such Notice is given at least ten (10) days before the date of sale. The proceeds from any such disposition, less all expenses incurred in connection with the taking of possession, holding and selling of such property (including, reasonable attorneys' fees) shall be applied as a credit against the indebtedness which is secured by the security interest granted in SECTION 7.2. Any surplus shall be paid to Tenant or as otherwise required by law and Tenant shall pay any deficiency to Landlord, as Additional Charges, upon demand.

12.2 REMEDIES. None of (a) the termination of this Agreement pursuant to SECTION 12.1; (b) the repossession of the Property or any portion thereof; (c) the failure of Landlord to re-let the Property or any portion thereof; nor (d) the reletting of all or any of portion of the Property, shall relieve Tenant of its liability and obligations hereunder, all of which shall survive any such termination, repossession or re-letting. In the event of any such termination, Tenant shall forthwith pay to Landlord all Rent due and

payable hereunder through and including the date of such termination. Thereafter, Tenant, until the end of what would have been the Term of this Agreement in the absence of such termination, shall be liable to Landlord for, and shall pay to Landlord, as current damages, the Rent and other charges which would be payable hereunder for the remainder of the Term had such termination not occurred, less the net proceeds, if any, of any re-letting of the Property, after deducting all expenses in connection with such reletting, including, without limitation, all repossession costs, brokerage commissions, legal expenses, attorneys' fees, advertising, expenses of employees, alteration costs and expenses of preparation for such reletting. Tenant shall pay such current damages to Landlord monthly on the days on which the Minimum Rent would have been payable hereunder if this Agreement had not been so terminated with respect to such of the Property.

At any time after such termination, whether or not Landlord shall have collected any such current damages, as liquidated final damages beyond the date of such termination, at Landlord's election, Tenant shall pay to Landlord either (a) an amount equal to the excess, if any (discounted to present value at the Prime Rate), of the Rent and other charges which would be payable hereunder from the date of such termination (assuming that, for the purposes of this paragraph, annual payments by Tenant on account of Impositions would be the same as payments required for the immediately preceding twelve calendar months, or if less than twelve calendar months have expired since the Commencement Date, the payments required for such lesser period projected to an annual amount) for what would be the then unexpired term of this Agreement if the same remained in effect, less the Fair Market Rental for the same period, or (b) an amount equal to the lesser of (i) the Rent and other charges that would have been payable for the balance of the Term had it not been terminated, and (ii) the aggregate of the Rent and other charges accrued in the nine (9) months ended next prior to such termination. In the event this Agreement is so terminated prior to the expiration of the first full year of the Term, the liquidated damages which Landlord may elect to recover pursuant to clause (b) (ii) of this paragraph shall be calculated as if such termination had occurred on the first anniversary of the Commencement Date. Nothing contained in this Agreement shall, however, limit or prejudice the right of Landlord to prove and obtain in proceedings for bankruptcy or insolvency an amount equal to the maximum allowed by any statute or rule of law in effect at the time when, and governing the proceedings in which, the damages are to be proved, whether or not the amount be greater than, equal to, or less than the amount of the loss or damages referred to above.

In case of any Event of Default, re-entry, expiration and dispossession by summary proceedings or otherwise, Landlord may (a) relet the Property as to which this Agreement is so terminated or any part or parts thereof, either in the name of Landlord or otherwise, for a term or terms which may at Landlord's option, be equal to, less than or exceed the period which would otherwise have constituted the balance of the Term and may grant concessions or free rent to the extent that Landlord considers advisable and necessary to relet the same, and (b) may make such reasonable alterations, repairs and decorations in the Property or any portion thereof as Landlord, in its sole and absolute discretion, considers advisable and necessary for the purpose of reletting the Property; and the making of such alterations, repairs and decorations shall not operate or be construed to release Tenant from liability hereunder as aforesaid. Landlord shall in no event be liable in any way whatsoever for any failure to relet all or any portion of the Property, or, in the event that the Property is relet, for failure to collect the rent under such reletting. To the maximum extent permitted by law, Tenant hereby expressly waives any and all rights of redemption granted under any present or future laws in the event of Tenant being evicted or dispossessed, or in the event of Landlord obtaining possession of the Property, by reason of the violation by Tenant of any of the covenants and conditions of this Agreement.

12.3 TENANT'S WAIVER. IF THIS AGREEMENT IS TERMINATED PURSUANT TO SECTION 12.1 OR 12.2, TENANT WAIVES, TO THE EXTENT PERMITTED BY LAW, ANY RIGHT TO A TRIAL BY JURY IN THE EVENT OF SUMMARY PROCEEDINGS TO ENFORCE THE REMEDIES SET FORTH IN THIS ARTICLE 12, AND THE BENEFIT OF ANY LAWS NOW OR HEREAFTER IN FORCE EXEMPTING PROPERTY FROM LIABILITY FOR RENT OR FOR DEBT.

12.4 APPLICATION OF FUNDS. Any payments received by Landlord under any of the provisions of this Agreement during the existence or continuance of any Default or Event of Default (and any payment made to Landlord rather than Tenant due to the existence of any Default or Event of Default) shall be applied to Tenant's obligations under this Agreement in such order as Landlord may determine or as may be required by Applicable Law.

12.5 LANDLORD'S RIGHT TO CURE TENANT'S DEFAULT. If a Default shall have occurred and be continuing, Landlord, after Notice to Tenant (which Notice shall not be required if Landlord shall reasonably determine in good faith immediate action is necessary to protect person or property), without waiving or releasing any obligation of Tenant and without waiving or releasing any Default, may (but shall not be obligated to), at any time thereafter, make such payment or perform such act for the account and at the expense of Tenant, and may, to the maximum extent permitted by law, enter upon the Property or any portion thereof for such purpose and take all such action thereon as, in Landlord's sole and absolute discretion, may be necessary or appropriate therefor. No such entry shall be deemed an eviction of Tenant. All reasonable costs and expenses (including, without limitation, reasonable attorneys' fees) incurred by Landlord in connection therewith (except to the extent such costs and expenses arise out of the negligence or wilful misconduct of Landlord or its agents), together with interest thereon (to the extent permitted by law) at the Overdue Rate from the date such sums are paid by Landlord until repaid, shall be paid by Tenant to Landlord, on demand.

ARTICLE 13
HOLDING OVER

Any holding over by Tenant after the expiration or sooner termination of this Agreement shall be treated as a daily tenancy at sufferance at a rate equal to one and one-half times the greater of the Fair Market Rental Value or the Minimum Rent and the Additional Rent then in effect plus any other charges herein provided (prorated on a daily basis). Tenant shall also pay to Landlord all actual damages sustained by reason of any such holding over. Otherwise, such holding over shall be on the terms and conditions set forth in this Agreement, to the extent applicable. Nothing contained herein shall constitute the consent, express or implied, of Landlord to the holding over of Tenant after the expiration or earlier termination of this Agreement.

ARTICLE 14
LANDLORD'S DEFAULT

Landlord shall not be deemed to be in default in the performance of any of its obligations hereunder unless it shall fail to perform such obligations and such failure shall continue for a period of thirty (30) days or such additional time as is reasonably required to correct any such default after Notice has been given by Tenant to Landlord specifying the nature of Landlord's alleged default. Tenant shall have no right to terminate this Agreement for any default by Landlord hereunder and no right, for any such default, to offset or counterclaim against any Rent due hereunder. In no event shall Landlord ever be liable to Tenant for any punitive damages or for any loss of business or any other indirect, special or consequential damages suffered by Tenant from whatever cause.

ARTICLE 15
PURCHASE OF LEASED PROPERTY

In the event Tenant shall purchase the Property from Landlord pursuant to the terms of this Agreement, Landlord shall, upon receipt from Tenant of the applicable purchase price by wire transfer of immediately available federal funds, together with full payment of any unpaid Rent and other charges due and payable with respect to any period ending on or before the date of the purchase, deliver to Tenant a

quitclaim deed and other instruments, conveying the entire interest of Landlord in and to the Property to Tenant, free and clear of all encumbrances created through the act or omission of Landlord other than (i) Permitted Encumbrances and such other liens, if any, which Tenant has agreed in writing to accept and take title subject to, and (ii) encumbrances imposed on the Property under SECTION 5.5. The Property shall be conveyed to Tenant on an "as is" basis and in its "as-is" physical condition. The closing of any such sale shall be subject to all terms and conditions with respect thereto set forth in this Agreement and expenses of such conveyance, including, without limitation, all transfer and sales taxes, documentary fees, the fees and expenses of counsel to Landlord and the cost of any title examination or title insurance, shall be paid by Tenant.

ARTICLE 16
SUBLETTING AND ASSIGNMENT

16.1 SUBLETTING AND ASSIGNMENT. Tenant shall not, without the prior written consent of Landlord, assign, mortgage, pledge, hypothecate, encumber or otherwise transfer this Agreement or sublease (which term shall be deemed to include the granting of concessions, licenses and the like), all or any part of the Property or suffer or permit this Agreement or the leasehold estate created hereby or any other rights arising under this Agreement to be assigned, transferred, mortgaged, pledged, hypothecated or encumbered, in whole or in part, whether voluntarily, involuntarily or by operation of law, or permit the use or occupancy of the Property by anyone other than Tenant, or the Property to be offered or advertised for assignment or subletting.

Notwithstanding the foregoing, Tenant may, without the need for Landlord's consent, assign its interest in this Lease (a "PERMITTED ASSIGNMENT") to any Affiliated Person so long as (i) Tenant shall promptly furnish Landlord with fully executed counterparts of any such assignment after consummation thereof which assignment shall include an agreement by the assignee, in form reasonably satisfactory to Landlord, to be bound by all of the terms of this Lease, and (ii) there shall not be an Event of Default at the effective date of such Permitted Assignment. Tenant shall also be permitted, without the need for Landlord's consent but upon prior notice to Landlord (including delivery of a copy of such sublease), to enter into any sublease with any Affiliated Party provided that such sublease shall expire upon any event pursuant to which the sublessee thereunder shall cease to be an Affiliated Party. Any assignment or sublease to an Affiliated Party may, at Landlord's election, be deemed terminated if during the term of this Lease such assignee or sublessee shall cease to be an Affiliated Party.

If this Agreement is assigned or if the Property or any part thereof is sublet, Landlord may collect the rents from such assignee or subtenant, as the case may be, and apply the net amount collected to the Rent herein reserved, but no such collection shall be deemed a waiver of the provisions set forth in the first paragraph of this SECTION 16.1, the acceptance by Landlord of such assignee or subtenant, as the case may be, as a tenant, or a release of Tenant from the future performance by Tenant of its covenants, agreements or obligations contained in this Agreement.

Provided that Tenant shall have complied with the provisions of the final paragraph of this SECTION 16.1, so long as there shall exist no Event of Default, Landlord shall not unreasonably withhold, condition or delay its consent to one or more subleases of all or a portion of the Property for the balance of the term of this Lease providing that: (I) the proposed subtenant(s) have a good reputation and financial standing; (II) in Landlord's reasonable judgment, the business of the proposed subtenant(s) is within the definition of the Primary Intended Use; (III) the proposed subtenant(s) are not governmental agencies or occupants; (IV) Tenant shall, at its expense, perform all work necessary to divide the sublet premises from the remainder of the Improvements; and (V) Landlord has received sufficient information from Tenant to make a reasonable determination regarding the requirements set forth in clauses (I) and (II).

If the rent and other sums (including, without limitation, all monetary payments plus the reasonable value of any services performed or any other thing of value given by any assignee or subtenant in

consideration of such assignment or sublease), either initially or over the term of any assignment or sublease other than a Permitted Assignment or a sublease or assignment to an Affiliated Party (collectively an "UNRELATED TRANSACTION"), payable by such assignee or subtenant exceed the sum of (a) Minimum Rent, plus (b) Additional Rent and other charges called for hereunder with respect to the space assigned or sublet, plus (c) the cost of any leasehold improvements to the space to be subleased or assigned performed for such subtenant or assignee, plus (d) the then unamortized cost substantiated by appropriate information supplied to Landlord by Tenant of any leasehold improvements performed to the space to be sublet or assigned by Tenant at the request of such subtenant or assignee, plus (e) any reasonable brokerage commissions and attorneys fees incurred by Tenant in connection with such sublease or assignment or in obtaining Landlord's consent (all such costs to be amortized over the term of such sublease or assignment), Tenant shall pay to Landlord as Additional Rent fifty percent (50%) of such excess payable monthly at the time for payment of Minimum Rent. Nothing in this paragraph shall be deemed to abrogate the provisions of this Article 16 and Landlord's acceptance of any sums pursuant to this paragraph shall not be deemed a granting of consent to any assignment of the Lease or sublease of all or any portion of the Property.

No subletting or assignment shall in any way impair the continuing primary liability of Tenant hereunder, and no consent to any subletting or assignment in a particular instance shall be deemed to be a waiver of the prohibition set forth in this SECTION 16.1. No assignment, subletting or occupancy shall be permitted for any use other than the Primary Intended Use. Any subletting, assignment or other transfer of Tenant's interest under this Agreement in contravention of this SECTION 16.1 shall be voidable at Landlord's option.

In the event that Tenant shall intend to enter into any Unrelated Transaction which is either (A) an assignment or (B) a sublease which together with any other related sublease shall encompass not less than fifty percent of the rentable area of the Facility, then Tenant shall, not sooner than one hundred and twenty (120) days, and not later than thirty (30) days, prior to the proposed effective date of such Unrelated Transaction, give Landlord notice of such intent, identifying the prospective subtenant or assignee and setting forth the proposed terms of such sublease or assignment and Landlord may elect to terminate this Lease by giving notice to Tenant of such election not later than thirty (30) days after receiving notice of such intent from Tenant, whereupon this Lease shall terminate on what would have been the effective date of such sublease or assignment as if this Lease had expired by effluxion of time. If Tenant shall not enter into such sublease or assignment within such following thirty (30) day period and shall still desire to enter into any sublease or assignment, or if Tenant shall change the terms and conditions thereof following the date of Tenant's notice to Landlord, the first sentence of this paragraph shall again become applicable.

16.2 REQUIRED SUBLEASE PROVISIONS. Any sublease of all or any portion of the Property shall provide (a) that it is subject and subordinate to this Agreement and to the matters to which this Agreement is or shall be subject or subordinate; (b) that in the event of termination of this Agreement or reentry or dispossession of Tenant by Landlord under this Agreement, Landlord may, at its option, terminate such sublease or take over all of the right, title and interest of Tenant, as sublessor under such sublease, and such subtenant shall, at Landlord's option, attorn to Landlord pursuant to the then executory provisions of such sublease, except that neither Landlord nor any Facility Mortgagee, as holder of a mortgage or as Landlord under this Agreement, if such mortgagee succeeds to that position, shall (i) be liable for any act or omission of Tenant under such sublease, (ii) be subject to any credit, counterclaim, offset or defense which theretofore accrued to such subtenant against Tenant, (iii) be bound by any previous modification of such sublease not consented to in writing by Landlord or by any previous prepayment of more than one (1) month's Rent, (iv) be bound by any covenant of Tenant to undertake or complete any construction of the Property or any portion thereof, (v) be required to account for any security deposit of the subtenant other than any security deposit actually delivered to Landlord by Tenant, (vi) be bound by any obligation to make any payment to such subtenant or grant any credits, (vii) be responsible for any monies owing by Tenant to the credit of such subtenant, or (viii) be required to remove any Person occupying any portion of the Property; and (c) that in the event that such subtenant receives a written Notice from Landlord or any

Facility Mortgagee stating that an Event of Default has occurred and is continuing, such subtenant shall thereafter be obligated to pay all rentals accruing under such sublease directly to the party giving such Notice or as such party may direct. All rentals received from such subtenant by Landlord or the Facility Mortgagee, as the case may be, shall be credited against the amounts owing by Tenant under this Agreement and such sublease shall provide that the subtenant thereunder shall, at the request of Landlord, execute a suitable instrument in confirmation of such agreement to attorn. An original counterpart of each such sublease and assignment and assumption, duly executed by Tenant and such subtenant or assignee, as the case may be, in form and substance reasonably satisfactory to Landlord, shall be delivered promptly to Landlord and in the case of an assignment, the assignee shall assume in writing and agree to keep and perform all of the terms of this Agreement on the part of Tenant to be kept and performed and shall be, and become, jointly and severally liable with Tenant for the performance thereof.

The provisions of this SECTION 16.2 shall not be deemed a waiver of the provisions set forth in the first paragraph of SECTION 16.1.

16.3 SUBLEASE LIMITATION. Anything contained in this Agreement to the contrary notwithstanding, Tenant shall not sublet the Property on any basis such that the rental to be paid by any sublessee thereunder would be based, in whole or in part, on either (a) the income or profits derived by the business activities of such sublessee, or (b) any other formula such that any portion of such sublease rental would fail to qualify as "rents from real property" within the meaning of Section 856(d) of the Code, or any similar or successor provision thereto.

ARTICLE 17
STOPPEL CERTIFICATES AND FINANCIAL STATEMENTS

17.1 ESTOPPEL CERTIFICATES. Upon not less than ten (10) days' prior Notice by Landlord, Tenant shall (and upon not less than ten (10) days' prior Notice by Tenant Landlord shall) execute, acknowledge and deliver a statement in writing certifying that this Agreement is unmodified and in full force and effect (or, if there have been any modifications, that this Agreement is in full force and effect as modified and stating the modifications and, if there are any defenses, offsets or counterclaims, setting them forth in reasonable detail) and the dates to which the Minimum Rent and Additional Rent and other charges have been paid; and in the case Tenant is the party from whom the certification is sought, that it has no defenses, offsets or counterclaims against its obligations to pay the Minimum Rent and Additional Rent and other charges have been paid, and any other matter pertaining to this Agreement which is the subject of a reasonable inquiry. Any such statement delivered pursuant to this Section 17.1 may be relied upon by any prospective purchaser or mortgagee of the Property, or any prospective assignee of such mortgage, or by any lender or Government Agency doing or proposing to do business with Tenant or any prospective assignee or sublessee of Tenant Any certification may be limited to the knowledge of the individual executing the certification provided such individual shall be familiar with this Agreement and the condition of the Property.

17.2 FINANCIAL STATEMENTS.

Tenant shall furnish the following statements to Landlord:

(a) within forty-five (45) days after each of the first three quarters of any Fiscal Year, the most recent Consolidated Financials and the most recent unaudited financial statements of Tenant, in each case accompanied by the Financial Officer's Certificate;

(b) within ninety (90) days after the end of each Fiscal Year, the most recent Consolidated Financials for such year, including the most recent financial statements of Tenant, in each case certified by Ernst & Young LLP or another independent certified public accountant reasonably satisfactory to Landlord and accompanied by a Financial Officer's Certificate;

(c) promptly after the sending thereof, copies of all reports which Tenant sends to its security holders generally, and (if applicable) copies of all periodic reports which Tenant and/or any Guarantor files with the SEC or any stock exchange on which its shares are listed or traded;

(d) promptly after the delivery thereof to Tenant or its management, a copy of any management letter or written report prepared by the certified public accountants with respect to the financial condition, operations, business or prospects of Tenant;

(e) at any time and from time to time upon not less than twenty (20) days Notice from Landlord any Consolidated Financials or any other financial reporting information required to be filed by Landlord with any securities and exchange commission, the SEC or any successor agency, or any other governmental authority, or required pursuant to any order issued by any court, governmental authority or arbitrator in any litigation to which Landlord is a party, for purposes of compliance therewith provided to the extent Tenant incurs any costs in connection with the preparation of any such information in excess of the cost incurred in preparing the information required in Section 17.2(a)-(d), then Landlord shall pay the reasonable costs Tenant shall so incur, provided Tenant shall give Landlord Notice of a reasonable estimate thereof prior to incurring such costs; and

(f) promptly, upon Notice from Landlord, such other information concerning the business, financial condition and affairs of Tenant as Landlord may reasonably request from time to time.

Landlord may at any time, and from time to time, provide any Facility Mortgagee with copies of any of the foregoing statements.

ARTICLE 18
LANDLORD'S RIGHT TO INSPECT

Tenant shall permit Landlord and its authorized representatives to inspect the Property during usual business hours upon not less than twenty-four (24) hours' notice, and to make such repairs as Landlord is permitted or required to make pursuant to the terms of this Agreement, provided that any inspection or repair by Landlord or its representatives will not unreasonably interfere with Tenant's use and operation of the Property and further provided that in the event of an emergency, as determined by Landlord in its sole discretion, prior Notice shall not be necessary.

ARTICLE 19
APPRAISAL

19.1 APPRAISAL PROCEDURE. In the event that it becomes necessary to determine the Fair Market Value of the Property for any purpose of this Agreement and the parties cannot agree thereon, such Fair Market Value shall be determined upon the written demand of either party in accordance with the following procedure.

The party requesting an appraisal, by Notice given within thirty (30) days after the date of the event which requires or permits such procedure, shall appoint a Qualified Appraiser. The other party, by Notice given within fifteen (15) days after receipt of such Notice appointing the first Qualified Appraiser, may appoint a second Qualified Appraiser. If the other party fails to appoint the second Qualified Appraiser within such fifteen (15) day period, such party shall have waived its right to appoint a Qualified Appraiser, the first Qualified Appraiser shall appoint a second Qualified Appraiser within fifteen (15) days thereafter and the Fair Market Value shall be determined by the Qualified Appraisers as set forth below.

The two Qualified Appraisers shall thereupon endeavor to agree upon the Fair Market Value. If the two Qualified Appraisers so named cannot agree upon such value within thirty (30) days after the designation of the second such appraiser, each such appraiser shall, within five (5) days after the expiration

of such thirty (30) day period, submit his appraisal of fair market value to the other appraiser in writing, and if the fair market values set forth in such appraisals vary by five percent (5%) or less of the greater value, the fair market value shall be determined by calculating the average of the two fair market values determined by the two appraisers.

If the Fair Market Value set forth in the two appraisals vary by more than five percent (5%) of the greater value, the two Qualified Appraisers shall select a third Qualified Appraiser within an additional fifteen (15) days following the expiration of the aforesaid five (5) day period. If the two appraisers are unable to agree upon the appointment of a third appraiser within such fifteen (15) day period, either party may, upon written notice to the other, request that such appointment be made by the then President (or equivalent officer) of the State's Chapter of the American Institute of Real Estate Appraisers, or his or her designee or, if there is no such organization or if such individual declines to make such appointment, by any state or Federal court of competent jurisdiction for the State.

The third Qualified Appraiser shall determine Fair Market Value by selecting the Fair Market Value of one of the two other Qualified Appraisers.

In the event that any appraiser appointed hereunder does not or is unable to perform his or her obligation hereunder, then the party or the appraisers appointing such appraiser shall have the right to appoint a substitute Qualified Appraiser, but if the party or the appraisers who have the right to appoint a substitute Qualified Appraiser fail to do so within ten (10) days after written notice from the other party (or either party in the event such appraiser was appointed by the other appraisers) either party may, upon written notice to the party having the right to appoint a substitute Qualified Appraiser, request that such appointment be made by such officer of the American Institute of Real Estate Appraisers or court of competent jurisdiction as described above; PROVIDED, HOWEVER, that a party who has the right to appoint an appraiser or a substitute appraiser shall have the right to make such appointment only up until the time such appointment is made by such officer or court.

In connection with the appraisal process, Tenant shall provide the appraisers full access during normal business hours to examine the Property, the books, records and files of Tenant and all agreements, leases and other operating agreements relating to the Property.

The costs (other than Landlord's counsel fees) of each such appraisal shall be borne by Tenant and shall be Additional Rent. Upon determining such value, the appraisers shall promptly notify Landlord and Tenant in writing of such determination. If any party shall fail to appear at the hearings appointed by the appraisers, the appraisers may act in the absence of such party.

The determination of the Qualified Appraisers made in accordance with the foregoing provisions shall be final and binding upon the parties, such determination may be entered as an award in arbitration in a court of competent jurisdiction, and judgment thereon may be entered.

19.2 LANDLORD'S RIGHT TO APPRAISAL. Landlord shall have the right, exercisable not more than once during the Term, to appoint a Qualified Appraiser to perform a complete appraisal of the Property, which appraisal shall meet all requirements of any state or Federal bank regulatory authority that Landlord considers relevant or any Facility Mortgagee. The costs of each such appraisal shall be borne by Tenant and shall be included as Additional Rent.

ARTICLE 20
REPRESENTATIONS AND WARRANTIES

20.1 REPRESENTATIONS OF TENANT. To induce Landlord to enter into this Agreement, Tenant represents and warrants to Landlord as follows:

20.1.1 STATUS AND AUTHORITY OF TENANT. Tenant is a corporation duly organized, validly existing and in corporate good standing under the laws of its state of incorporation. Tenant has all requisite

power and authority under the laws of its state of formation and its charter documents to enter into and perform its obligations under this Agreement and to consummate the transactions contemplated hereby. Tenant has duly qualified to transact business in each jurisdiction in which the nature of the business conducted by it requires such qualification.

20.1.2 ACTION OF TENANT. Tenant has taken all necessary action to authorize the execution, delivery and performance of this Agreement, and this Agreement constitutes the valid and binding obligation and agreement of Tenant, enforceable against Tenant in accordance with its terms, except as enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium or similar laws of general application affecting the rights and remedies of creditors and equitable principles.

20.1.3 NO VIOLATIONS OF AGREEMENTS. Neither the execution, delivery or performance of this Agreement by Tenant, nor compliance with the terms and provisions hereof, will result in any breach of the terms, conditions or provisions of, or conflict with or constitute a default under, or result in the creation of any lien, charge or encumbrance upon the Property pursuant to the terms of any indenture, mortgage, deed of trust, note, evidence of indebtedness or any other material agreement or instrument by which Tenant is bound.

20.1.4 LITIGATION. Tenant has received no written notice of and, to Tenant's knowledge, no action or proceeding is pending or threatened and no investigation looking toward such an action or proceeding has begun, which questions the validity of this Agreement or any action taken or to be taken pursuant hereto, will result in any material adverse change in the business, operation, affairs or condition of the Property, will result in or subject the Property to a material liability, or involves condemnation or eminent domain proceedings against any material part of the Property.

20.1.5 DISCLOSURE. To Tenant's knowledge, there is no fact or condition which materially and adversely affects the condition of the Property which has not been set forth in this Agreement or in the other documents, certificates or statements furnished to Landlord in connection with the transactions contemplated hereby.

20.1.6 COMPLIANCE WITH LAW. Except as disclosed in writing to Landlord, to Tenant's knowledge, the Property and the use and operation thereof do not violate any material federal, state, municipal and other governmental statutes, ordinances, by-laws, rules, regulations or any other legal requirements, including, without limitation, those relating to construction, occupancy, zoning, adequacy of parking, environmental protection, occupational health and safety and fire safety applicable thereto; and there are presently in effect all material licenses, permits and other authorizations necessary for the current use, occupancy and operation thereof. Tenant has not received written notice of any threatened request, application, proceeding, plan, study or effort which would materially adversely affect the present use or zoning of the Property or which would modify or realign any adjacent street or highway in a manner which would materially adversely affect the use and operation of the Property.

20.1.7 HAZARDOUS SUBSTANCES. Except as disclosed to Landlord or as described in any environmental report delivered to Landlord, to Tenant's knowledge, none of Tenant nor any tenant or other occupant or user of the Property, or any portion thereof, has stored or disposed of (or engaged in the business of storing or disposing of) or has released or caused the release of any Hazardous Substances on the Property, the removal of which is required or the maintenance of which is prohibited or penalized by any Applicable Law, and, to Tenant's knowledge, except as disclosed to Landlord or as described in any environmental report delivered to Landlord, the Property is free from any such Hazardous Substances, except any such materials maintained in accordance with Applicable Law.

20.1.8 GENERALLY. For purposes of this Section 20.1, Tenant's knowledge shall be limited to the actual knowledge of Frederick A. Eustis, III or John S. McBride.

20.2 REPRESENTATIONS OF LANDLORD. To induce Tenant to enter in this Agreement, Landlord represents and warrants to Tenant as follows:

20.2.1 STATUS AND AUTHORITY OF LANDLORD. Landlord is a Maryland real estate investment trust duly organized, validly existing and in good standing under the laws of the State of Maryland, and has all requisite power and authority under the laws of such state and under its charter documents to enter into and perform its obligations under this Agreement and to consummate the transactions contemplated hereby. Landlord has duly qualified and is in good standing as a trust or unincorporated business association in each jurisdiction in which the nature of the business conducted by it requires such qualification.

20.2.2 ACTION OF LANDLORD. Landlord has taken all necessary action to authorize the execution, delivery and performance of this Agreement, and upon the execution and delivery of this Agreement by Landlord constitutes the valid and binding obligation and agreement of Landlord, enforceable against Landlord in accordance with its terms, except as enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium or similar laws of general application affecting the rights and remedies of creditors and equitable principles.

20.2.3 NO VIOLATIONS OF AGREEMENTS. Neither the execution, delivery or performance of this Agreement by Landlord, nor compliance with the terms and provisions hereof, will result in any breach of the terms, conditions or provisions of, or conflict with or constitute a default under, or result in the creation of any lien, charge or encumbrance upon any property or assets of Landlord pursuant to the terms of any indenture, mortgage, deed of trust, note, evidence of indebtedness or any other agreement or instrument by which Landlord is bound.

20.2.4 LITIGATION. No investigation, action or proceeding is pending and, to Landlord's actual knowledge, no action or proceeding is threatened and no investigation looking toward such an action or proceeding has begun, which questions the validity of this Agreement or any action taken or to be taken pursuant hereto.

20.2.5 GENERALLY. For purposes of this Section 20.2, Landlord's knowledge shall be limited to the actual knowledge of David Hegarty.

ARTICLE 21
FACILITY MORTGAGES

21.1 LANDLORD MAY GRANT LIENS. Without the consent of Tenant, Landlord may, subject to the terms and conditions set forth in this SECTION 21.1, from time to time, directly or indirectly, create or otherwise cause to exist any lien, encumbrance or title retention agreement ("ENCUMBRANCE") upon the Property, or any portion thereof or interest therein, whether to secure any borrowing or other means of financing or refinancing. Any such Encumbrance shall include the right to prepay (whether or not subject to a prepayment penalty) and shall provide (subject to SECTION 21.2 below) that it is subject to the rights of Tenant under this Agreement, including the rights of Tenant to acquire the Property pursuant to the applicable provisions of this Agreement.

21.2 SUBORDINATION OF LEASE. Subject to SECTION 21.1, this Agreement, any and all rights of Tenant hereunder, are and shall be subject and subordinate to any ground or master lease, and all renewals, extensions, modifications and replacements thereof, and to all mortgages and deeds of trust, which may now or hereafter affect the Property, or any of them, or any improvements thereon and/or any of such leases, whether or not such mortgages or deeds of trust shall also cover other lands and/or buildings and/or leases, to each and every advance made or hereafter to be made under such mortgages and deeds of trust, and to all renewals, modifications, replacements and extensions of such leases and such mortgages and deeds of trust and all consolidations of such mortgages and deeds of trust, provided that, with respect to any such lease, mortgage or deed of trust, Landlord shall deliver to Tenant an agreement by such lessor or

holder in a commercially reasonable form to the effect that Tenant's rights hereunder shall not be disturbed by such lessor or holder so long as there exists no Event of Default. This section shall be self-operative and no further instrument of subordination shall be required. In confirmation of such subordination, Tenant shall promptly execute, acknowledge and deliver any instrument that Landlord, the lessor under any such lease or the holder of any such mortgage or the trustee or beneficiary of any deed of trust or any of their respective successors in interest may reasonably request to evidence such subordination. Any lease to which this Agreement is, at the time referred to, subject and subordinate is herein called "SUPERIOR LEASE" and the lessor of a Superior Lease or its successor in interest at the time referred to, is herein called "SUPERIOR LANDLORD" and any mortgage or deed of trust to which this Agreement is, at the time referred to, subject and subordinate, is herein called "SUPERIOR MORTGAGE" and the holder, trustee or beneficiary of a Superior Mortgage is herein called "SUPERIOR MORTGAGEE".

If any Superior Landlord or Superior Mortgagee or the nominee or designee of any Superior Landlord or Superior Mortgagee shall succeed to the rights of Landlord under this Agreement, whether through possession or foreclosure action or delivery of a new lease or deed, or otherwise, then at the request of such party so succeeding to Landlord's rights (herein called "SUCCESSOR LANDLORD") and upon such Successor Landlord's written agreement to accept Tenant's attornment, Tenant shall attorn to and recognize such Successor Landlord as Tenant's landlord under this Agreement, and shall promptly execute and deliver any instrument that such Successor Landlord may reasonably request to evidence such attornment. Upon such attornment, this Agreement shall continue in full force and effect as a direct lease between the Successor Landlord and Tenant upon all of the terms, conditions and covenants as are set forth in this Agreement, except that the Successor Landlord (unless formerly the landlord under this Agreement or its nominee or designee) shall not be (a) liable in any way to Tenant for any act or omission, neglect or default on the part of Landlord under this Agreement; (b) responsible for any monies owing by or on deposit with Landlord to the credit of Tenant; (c) subject to any counterclaim or setoff which theretofore accrued to Tenant against Landlord; (d) bound by any modification of this Agreement subsequent to such Superior Lease or Mortgage, or by any previous prepayment of Minimum Rent or Additional Rent for more than one (1) month, which was not approved in writing by the Superior Landlord or the Superior Mortgagee thereto; (e) liable to Tenant beyond the Successor Landlord's interest in the Property and the rents, income, receipts, revenues, issues and profits issuing from the Property; (f) responsible for the performance of any work to be done by the Landlord under this Agreement to render the Property ready for occupancy by Tenant; or (g) required to remove any Person occupying the Property or any part thereof, except if such person claims by, through or under the Successor Landlord. Tenant agrees at any time and from time to time to execute a suitable instrument in confirmation of Tenant's agreement to attorn, as aforesaid.

21.3 NOTICE TO MORTGAGEE AND GROUND LANDLORD. Subsequent to the receipt by Tenant of notice from any Person that it is a Facility Mortgagee, or that it is the ground lessor under a lease with Landlord, as ground lessee, which includes the Property as part of the demised premises, no notice from Tenant to Landlord shall be effective unless and until a copy of the same is given to such Facility Mortgagee or ground lessor, and the curing of any of Landlord's defaults by such Facility Mortgagee or ground lessor shall be treated as performance by Landlord.

ARTICLE 22
ADDITIONAL COVENANTS OF TENANT

22.1 CONDUCT OF BUSINESS. Tenant shall do or cause to be done all things necessary to preserve, renew and keep in full force and effect and in good standing its corporate existence and its rights and licenses necessary to conduct its business.

22.2 MAINTENANCE OF ACCOUNTS AND RECORDS. Tenant shall keep true records and books of account in which full, true and correct entries will be made of dealings and transactions in relation to the business and

affairs of Tenant in accordance with GAAP. Tenant shall apply accounting principles in the preparation of the financial statements of Tenant which, in the judgment of and the opinion of its independent public accountants, are in accordance with GAAP, except for changes approved by such independent public accountants.

22.3 NOTICE OF LITIGATION, POTENTIAL EVENT OF DEFAULT, ETC. Tenant shall give prompt Notice to Landlord of any litigation or any administrative proceeding to which it may hereafter become a party which involves a potential uninsured liability equal to or greater than Twenty-Five Thousand Dollars ($25,000) or which may otherwise result in any material adverse change in the business, operations, property, prospects, results of operation or condition, financial or other, of Tenant. Forthwith upon Tenant obtaining knowledge of any event or condition that would be required to be disclosed in a current report filed by Tenant on Form 8-K or in Part II of a quarterly report on Form 10-Q if Tenant were required to file such reports under the Securities Exchange Act of 1934, as amended, Tenant shall furnish Notice thereof to Landlord specifying the nature and period of existence thereof and what action Tenant has taken or is taking or proposes to take with respect thereto.

22.4 FINANCIAL CONDITION OF TENANT.

(a) Tenant shall at all times maintain current assets (excluding the Security Deposit) in excess of current liabilities by an amount at least equal to the Rent due for the following twelve months. The terms "current assets" and "current liabilities", respectively, shall mean all assets or liabilities, as the case may be, which should, in accordance with GAAP, be classified as current assets or current liabilities, as the case may be.

(b) Tenant shall at all times maintain Tangible Net Worth in an amount at least equal to the Rent due for the following twelve months.

22.5 PROHIBITED TRANSACTIONS. Tenant shall not permit to exist or enter into any agreement or arrangement whereby it engages in a transaction of any kind with any Affiliated Person (other than a wholly owned subsidiary) except on terms and conditions which are not less favorable to Tenant than those on which similar transactions between unaffiliated parties could fairly be expected to be entered into on an arms-length basis.

22.6 LIENS AND ENCUMBRANCES. Except as permitted by SECTION 7.1, subject to the provisions of ARTICLE 8 relating to Permitted Contests, Tenant shall not create or incur or suffer to be created or incurred or to exist any Lien on this Agreement, or its leasehold interest in the Property other than Permitted Encumbrances.

22.7 MERGER; SALE OF ASSETS; ETC. Except as otherwise expressly provided in this Agreement, Tenant shall not (a) sell, lease (as lessor or sublessor), transfer or otherwise dispose of, or abandon, more than 49% of its assets, regardless of the consideration, or any material portion of its assets (including capital stock) or business to any Person for less than the fair value thereof; (b) merge into or with or consolidate with any other Entity; or (c) allow a Change in Control of Tenant to occur PROVIDED, HOWEVER, that, notwithstanding the provisions of clauses (a), (b) or (c) preceding, Tenant may merge into or may sell all or substantially all of its assets to an Entity which shall in any case have both a positive operating cash flow for each of the preceding three years, both before and after giving effect to such merger or sale and any related transactions, and a Tangible Net Worth of $20,000,000 after giving effect to such merger or sale and any related transactions and which shall assume all of Tenant's obligations under this Agreement in form satisfactory to Landlord; provided however, that (i) if holders of the equity interest in Tenant prior to the merger shall collectively own not less than fifty-one percent (51%) of the equity interest in the Entity following and giving effect to the merger, then the positive operating cash flow requirement shall not be a requirement and (ii) if Tenant shall intend to merge into or to sell all or substantially all of its assets to an Entity which shall not meet the foregoing requirements then Tenant may, provided such merger or sale is to an independent third party and is made for a bonafide corporate purpose and not principally to allow

termination of this Agreement, elect by Notice to Landlord to purchase the Property. If Tenant shall make such election, then the closing of such transaction shall occur as of the date of such merger or sale (but in no event less than sixty (60) nor more than ninety (90) days following such Notice), Tenant shall pay the greater of Nine Millions Dollars ($9,000,000) or Fair Market Value to Landlord at closing, and upon payment thereof, this Agreement shall terminate.

ARTICLE 23
RIGHT OF FIRST REFUSAL TO PURCHASE

If at any time during the Term of this Agreement, Landlord intends to accept an offer or enter into an agreement to sell its entire interest in the Property, Landlord shall give Notice to Tenant in which it shall first offer to sell the Property to Tenant on the same terms and conditions which Landlord intends to accept. Landlord's Notice of such offer shall include the material terms under which Landlord intends to make such sale. Tenant shall have ten (10) days in which to respond to Landlord's offer. If Tenant elects to accept such offer, Tenant shall give Landlord Notice thereof within such 10-day period, and Landlord and Tenant shall, within fifteen (15) business days after Tenant's Notice, execute a purchase and sale agreement prepared by Landlord incorporating such terms and conditions and other mutually acceptable terms and provisions.

The provisions of the first paragraph of this Article 23 shall not apply to (i) any proposed transaction by Landlord with any Affiliated Person or (ii) any proposed transfer to any entity providing financing to Landlord or any foreclosure proceeding or lease or deed in lieu of foreclosure, or (iii) any proposed sale of the Property as part of a sale of a portfolio of properties (i.e., in a transaction pursuant to which the Property is to be sold together with at least one other property owned by Landlord or any Affiliated Person), but to the extent applicable prior to any such transaction the first paragraph hereof shall apply after the closing of such transaction.

It is expressly understood and agreed that time shall be of the essence with respect to the giving of such Notice by Tenant and the failure of Tenant to give such Notice within the time and in the manner hereinabove provided shall be a waiver of Tenant's rights pursuant to this Article 23. Any purchase of the Property by Tenant shall be made in accordance with the provisions of ARTICLE 15.

ARTICLE 24
MISCELLANEOUS

24.1 LIMITATION ON PAYMENT OF RENT. All agreements between Landlord and Tenant herein are hereby expressly limited so that in no contingency or event whatsoever, whether by reason of acceleration of Rent, or otherwise, shall the Rent or any other amounts payable to Landlord under this Agreement exceed the maximum permissible under applicable law, the benefit of which may be asserted by Tenant as a defense, and if, from any circumstance whatsoever, fulfillment of any provision of this Agreement, at the time performance of such provision shall be due, shall involve transcending the limit of validity prescribed by law, or if from any circumstances Landlord should ever receive as fulfillment of such provision such an excessive amount, then, IPSO FACTO, the amount which would be excessive shall be applied to the reduction of the installment(s) of Minimum Rent next due and not to the payment of such excessive amount. This provision shall control every other provision of this Agreement and any other agreements between Landlord and Tenant.

24.2 NO WAIVER. No failure by Landlord to insist upon the strict performance of any term hereof or to exercise any right, power or remedy consequent upon a breach thereof, and no acceptance of full or partial payment of Rent during the continuance of any such breach, shall constitute a waiver of any such breach or of any such term. To the maximum extent permitted by law, no waiver of any breach shall affect

or alter this Agreement, which shall continue in full force and effect with respect to any other then existing or subsequent breach.

24.3 REMEDIES CUMULATIVE. To the maximum extent permitted by law, each legal, equitable or contractual right, power and remedy of Landlord, now or hereafter provided either in this Agreement or by statute or otherwise, shall be cumulative and concurrent and shall be in addition to every other right, power and remedy and the exercise or beginning of the exercise by Landlord of any one or more of such rights, powers and remedies shall not preclude the simultaneous or subsequent exercise by Landlord of any or all of such other rights, powers and remedies.

24.4 SEVERABILITY. Any clause, sentence, paragraph, section or provision of this Agreement held by a court of competent jurisdiction to be invalid, illegal or ineffective shall not impair, invalidate or nullify the remainder of this Agreement, but rather the effect thereof shall be confined to the clause, sentence, paragraph, section or provision so held to be invalid, illegal or ineffective, and this Agreement shall be construed as if such invalid, illegal or ineffective provisions had never been contained therein.

24.5 ACCEPTANCE OF SURRENDER. No surrender to Landlord of this Agreement or of the Property or any part thereof, or of any interest therein, shall be valid or effective unless agreed to and accepted in writing by Landlord and no act by Landlord or any representative or agent of Landlord, other than such a written acceptance by Landlord, shall constitute an acceptance of any such surrender.

24.6 NO MERGER OF TITLE. It is expressly acknowledged and agreed that it is the intent of the parties that there shall be no merger of this Agreement or of the leasehold estate created hereby by reason of the fact that the same Person may acquire, own or hold, directly or indirectly this Agreement or the leasehold estate created hereby and the fee estate or ground landlord's interest in the Property.

24.7 CONVEYANCE BY LANDLORD. If Landlord or any successor owner of all or any portion of the Property shall convey all or any portion there in accordance with the terms hereof other than as security for a debt, and the grantee or transferee thereof shall expressly assume all obligations of Landlord hereunder arising or accruing from and after the date of such conveyance or transfer, Landlord or such successor owner, as the case may be, shall thereupon be released from all future liabilities and obligations of Landlord under this Agreement with respect to the Property arising or accruing from and after the date of such conveyance or other transfer and all such future liabilities and obligations shall thereupon be binding upon the new owner.

24.8 QUIET ENJOYMENT. So long as Tenant shall pay the Rent as the same becomes due and shall comply with all of the terms of this Agreement, Tenant shall peaceably and quietly have, hold and enjoy the Property for the Term, free of hindrance or molestation by Landlord or anyone claiming by, through or under Landlord, but subject to (a) any Encumbrance permitted under Article 21 or otherwise permitted to be created by Landlord hereunder, (b) all Permitted Encumbrances, (c) liens as to obligations of Landlord that are either not yet due or which are being contested in good faith and by proper proceedings without threat to Tenant's leasehold estate, and (d) liens that have been consented to in writing by Tenant. Except as otherwise provided in this Agreement, no failure by Landlord to comply with the foregoing covenant shall give Tenant any right to cancel or terminate this Agreement or abate, reduce or make a deduction from or offset against the Rent or any other sum payable under this Agreement, or to fail to perform any other obligation of Tenant hereunder.

24.9 NON-LIABILITY OF TRUSTEES. TENANT ACKNOWLEDGES THAT THE DECLARATION, A COPY OF WHICH IS DULY FILED WITH THE DEPARTMENT OF ASSESSMENTS AND TAXATION OF THE STATE OF MARYLAND, PROVIDES THAT THE NAME "HUB RI PROPERTIES TRUST" REFERS TO THE TRUSTEES UNDER THE DECLARATION COLLECTIVELY AS TRUSTEES, BUT NOT INDIVIDUALLY OR PERSONALLY, AND THAT NO TRUSTEE, OFFICER, SHAREHOLDER, EMPLOYEE OR AGENT OF LANDLORD SHALL BE HELD TO ANY PERSONAL LIABILITY, JOINTLY OR SEVERALLY, FOR ANY OBLIGATION OF, OR CLAIM

AGAINST, LANDLORD. ALL PERSONS DEALING WITH LANDLORD, IN ANY WAY, SHALL LOOK ONLY TO THE ASSETS OF LANDLORD FOR THE PAYMENT OF ANY SUM OR THE PERFORMANCE OF ANY OBLIGATION. TENANT ACCEPTS AND AGREES TO COMPLY AND BE BOUND BY THE FOREGOING.

24.10 LANDLORD'S CONSENT OF TRUSTEES. Where provision is made in this Agreement for Landlord's consent and Landlord shall fail or refuse to give such consent, Tenant shall not be entitled to any damages for any withholding by Landlord of its consent, it being intended that Tenant's sole remedy shall be an action for specific performance or injunction, and that such remedy shall be available only in those cases where Landlord has expressly agreed in writing not unreasonably to withhold its consent.

24.11 MEMORANDUM OF LEASE. Neither Landlord nor Tenant shall record this Agreement. However, Landlord and Tenant shall promptly, upon the request of the other, enter into a short form memorandum of this Agreement, in form suitable for recording under the laws of the State in which reference to this Agreement, and all options contained herein, shall be made. Tenant shall pay all costs and expenses of recording such memorandum.

24.12 NOTICES.

(a) Any and all notices, demands, consents, approvals, offers, elections and other communications required or permitted under this Agreement shall be deemed adequately given if in writing and the same shall be delivered either in hand, by telecopier with written acknowledgment of receipt, or by mail or Federal Express or similar expedited commercial carrier, addressed to the recipient of the notice, postpaid and registered or certified with return receipt requested (if by mail), or with all freight charges prepaid (if by Federal Express or similar carrier).

(b) All notices required or permitted to be sent hereunder shall be deemed to have been given for all purposes of this Agreement upon the date of acknowledged receipt, in the case of a notice by telecopier, and, in all other cases, upon the date of receipt or refusal, except that whenever under this Agreement a notice is either received on a day which is not a Business Day or is required to be delivered on or before a specific day which is not a Business Day, the day of receipt or required delivery shall automatically be extended to the next Business Day.

(c) All such notices shall be addressed,

if to Landlord to:

Hub RI Properties Trust
400 Centre Street
Newton, Massachusetts 02158
Attn: Mr. David J. Hegarty
[Telecopier No. (617) 332-2261]

with a copy to:

Sullivan & Worcester LLP
One Post Office Square
Boston, Massachusetts 02109
Attn: Warren M. Heilbronner, Esq.
[Telecopier No. (617) 338-2880]

if to Tenant to:

Cytotherapeutics, Inc.
701 George Washington Highway
Lincoln, Rhode Island 02865
Attn: Vice President, Business Operations
[Telecopier No. (401) 334-9152]

with a copy to:

Cytotherapeutics, Inc.
701 George Washington Highway
Lincoln, Rhode Island 02865
Attn: General Counsel
[Telecopier No. (401) 333-0684]

(d) By notice given as herein provided, the parties hereto and their respective successor and assigns shall have the right from time to time and at any time during the term of this Agreement to change their respective addresses effective upon receipt by the other parties of such notice and each shall have the right to specify as its address any other address within the United States of America.

24.13 CONSTRUCTION. Anything contained in this Agreement to the contrary notwithstanding, all claims against, and liabilities of, Tenant or Landlord arising prior to any date of termination or expiration of this Agreement shall survive such termination or expiration. In no event shall Landlord be liable for any consequential damages suffered by Tenant as the result of a breach of this Agreement by Landlord. Neither this Agreement nor any provision hereof may be changed, waived, discharged or terminated except by an instrument in writing signed by the party to be charged. All the terms and provisions of this Agreement shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. Each term or provision of this Agreement to be performed by Tenant shall be construed as an independent covenant and condition. Time is of the essence with respect to the exercise of any rights of Tenant under this Agreement.

24.14 COUNTERPARTS; HEADINGS. This Agreement may be executed in two or more counterparts, each of which shall constitute an original, but which, when taken together, shall constitute but one instrument and shall become effective as of the date hereof when copies hereof, which, when taken together, bear the signatures of each of the parties hereto shall have been signed. Headings in this Agreement are for purposes of reference only and shall not limit or affect the meaning of the provisions hereof.

24.15 APPLICABLE LAW, ETC. Except as to matters regarding the internal affairs of Landlord and issues of or limitations on any personal liability of the shareholders and trustees of Landlord for obligations of Landlord, as to which the laws of the State of Maryland shall govern, this Agreement shall be interpreted, construed, applied and enforced in accordance with the laws of the State of Rhode Island.

To the maximum extent permitted by applicable law, any action to enforce, arising out of, or relating in any way to, any of the provisions of this Agreement may be brought and prosecuted in such court or courts located in The Commonwealth of Massachusetts as is provided by law; and the parties consent to the jurisdiction of said court or courts located in The Commonwealth of Massachusetts and to service of process by registered mail, return receipt requested, or by any other manner provided by law.

IN WITNESS WHEREOF, the parties have executed this Agreement as a sealed instrument as of the date above first written.

LANDLORD:

HUB RI PROPERTIES TRUST

By: /s/ DAVID J. HEGARTY

Its: President

TENANT:

CYTOTHERAPEUTICS, INC.

By: /s/ JOHN S. MCBRIDE

Its (Vice) President

EXHIBIT A

LEGAL DESCRIPTION

That certain lot or parcel of land with all the buildings and improvements thereon, situated on the southerly side of Washington Highway, in the Town of Lincoln, County of Providence, said parcel comprises Plat 29, Lot 300 and Parcel "A" as shown on that plan entitled "ALTA/ACSM Land Title Survey of Administrative Subdivision for CytoTherapeutics, Inc., Plat 29, Lots 150 & 300, Lincoln, Rhode Island, September 16, 1996, Scale: 1 inch equals 40 feet" by Marc N. Nyberg Associates, Inc. recorded September 20, 1996 at 12:19 p.m. as Map #234, more particularly bounded and described as follows:

Beginning at a point in the southerly line of said Washington Highway, said point being the most northeasterly corner of land now or formerly owned by Thomas M. & Judith G. Cullen and the most northwesterly corner of the parcel hereby described;

thence running easterly, following the southerly line of said Washington Highway, by a curve to the left, said curve having a radius of two thousand one hundred seventy-seven and 62/100 (2,177.62) feet, a central angle of 01 degrees 54 feet 36 inches, for a distance of seventy-two and 59/100 (72.59) feet to a point of tangency, said point being opposite state highway station 443+58.00 as shown on R.I. State Highway Plat No. 749;

thence running easterly, following the southerly line of said Washington Highway, five hundred ninety-six and 29/100 (596.29) feet;

thence running southeasterly, by a curve to the left, said curve having a radius of one hundred seventy-five and 00/100 (175.00) feet, a central angle of 24 degrees 48 feet 27 inches, for a distance of seventy-five and 77/100 (75.77) feet to a point of reverse curvature;

thence running southeasterly and southerly by a curve to the right, said curve having a radius of one hundred twenty-five and 00/100 (125.00) feet, a central angle of 41 degrees 24 feet 35 inches for a distance of ninety and 34/100 (90.34) feet to a point of tangency;

thence running southerly, two hundred fifty-one and 57/100 (251.57) feet, the last three lines bounding easterly on land now or formerly owned by Cullen, Inc.;

thence turning an interior angle of 90 degrees 00 feet 00 inches and running westerly, four hundred eighty-three and 38/100 (483.38) feet, the last line bounding southerly on remaining land now or lately of John J. Cullen and Roland Montigny;

thence turning an interior angle of 122 degrees 15 feet 15 inches and running northwesterly, four hundred seventy-four and 42/100 (474.42) feet to the point and place of beginning, the last line bounding westerly on other land now or lately of Thomas M. Cullen & Judith G. Cullen.

Said parcel contains 239,597 square feet or 5.500 aces.

EXHIBIT B

MINIMUM RENT

PERIOD	MINIMUM RENT
Original Term	
Commencement Date--12/31/2002	$62,500.00 per month
1/1/2003--12/31/2007	$78,125.00 per month
1/1/2008--12/31/2012	$97,656.25 per month
1/1/2013--6/30/2013	$122,070.30 per month
First Extended Term	
7/1/2013--12/31/2017	$122,070.30 per month
1/1/2018--12/31/2022	$152,587.86 per month
1/1/2023--6/30/2023	$190,734.83 per month
Second Extended Term	
7/1/2023--12/31/2027	$190,734.83 per month
1/1/2028--12/31/2032	$238,418.54 per month
1/1/2033--6/30/2033	$298,023.18 per month

EXHIBIT C
TENANT'S PERSONAL PROPERTY

Tenant's Trade Fixtures

ITEM #	DESCRIPTION	MANUFACTURER	QUANTITY	COST EACH	COST EXTENSION
1	Central glassware washer	AMSCO/Steris	1	61500	61500
2	Access control devices, cameras, VCRs	Various	1	67000	67000
3	Main Cagewasher-Model 4200	AMSCOS/Steris	1	51162	51162
4	Autoclave #1	Gatinge	1	18340	18340
5	Autoclave #2	Gatinge	1	32350	32350
6	Autoclave #3	Gatinge	1	18450	18450
7	Autoclave #4	Gatinge	1	18500	18500
8	Quarantine Cagewasher-Model 3500	AMSCO/Steris	1	22250	22250
9	Iceflakers	Scotsman	3	2149	6447
10	Undercounter Steam Scrubbers	Universal	3	4594	13782
11	Undercounter glasswashers	ASKO	2	750	1500
12	RO/D1 water production system	Millipore	1	27000	27000
13	Hazardous Materials Storage Shed	Safety Storage	1	19733	19733
14	Natural gas emergency generator-EAB	Olympian	1	21250	21250
15	Chemical fume hoods	HEMCO	5	5720	28600
16	Flammables storage cabinets	Safety Storage	6	400	2400
17	Laundry appliances	Maytag	1	900	900
18	Kitchen appliances-package	Various	1	5986	5986
19	Office furniture-package	Various	1	197500	197500
20	Freezers-package	Various	1	23520	23520
21	Window treatments-package	Various	1	17886	17886

ITEM #	DESCRIPTION	MANUFACTURER	QUANTITY	COST EACH	COST EXTENSION
22	Lab benches	Millwork One	1	205000	205000
23	Exhausted biosafety cabinets	Baker/Nuaire	5	6800	34000
24	Microisolator caging systems	Thoren	2	19500	39000
25	Bedding disposal units	TBJ/Nuaire	3	12500	37500
26	Telephone system package	NEC	1	77805	77805
27	Caging systems-package	Various	1	42300	42300
28	Surgery lights, animal care equipment	Various	1	87500	87500
29	Behavior testing equipment - animal care	Various	1	115000	115000
					1274151

Included but not scheduled are all portable lab and other devices that are typically mounted above or below countertops, which may or may not be powered by standard wall electrical recepticles.

Exhibit 10.68

CYTOTHERAPEUTICS, INC.
Two Richmond Square
Providence, RI 02906

Irving L. Weissman
Pathology B-257
Stanford Medical School
Stanford, CA 94305

Fred H. Gage
Laboratory of Genetics
10010 N. Torrey Pines Road
La Jolla, CA 92037

Re: Conduct of StemCells Research

Dear Irv and Rusty:

In connection with your agreeing to become consultants to CytoTherapeutics, Inc. ("CTI") pursuant to Consulting Agreements between each of you and the Company of even date herewith and the award to you pursuant to such Agreements of certain Options, we have agreed as follows regarding the conduct of certain research expected to have a material impact on the vesting of such options and a number of related matters. The provisions of this Agreement shall become effective on the closing of the acquisition of StemCells, Inc. ("SCI") by CTI.

1. Funding and Control of StemCells Research

a. SCI shall become the stem cells research arm of CTI. All stem cells research to be conducted or contracted for by CTI or SCI shall be conducted or contracted for through SCI; development work may be conducted or contracted for at CTI.

b. The stem cells research program to be conducted by SCI through June 30, 1999 shall be conducted as provided in the Research Plan (the "Research Plan") in the form attached hereto as Exhibit 1. All stem cells research shall be conducted in accordance with the Research Plan. Any changes in the Research Plan must be approved by the Research Committee (as defined below).

c. The Research Committee shall consist of two persons chosen by the Scientific Founders (initially, Weissman and Gage), two persons chosen by CTI (initially, Richard Rose and Seth Rudnick) and a fifth, independent member appointed by

the Scientific Founders, subject to the reasonable approval of CTI. The term "Scientific Founders" shall refer to two of you, provided, however, that if any one of you should resign without Good Reason or be terminated for Cause (as such terms are defined in your Consulting Agreements), the term Scientific Founders shall mean the remaining one of you.

d. The Research Committee shall meet at least quarterly to review progress under the Research Plan and make any adjustments to the Research Plan which the Committee deems necessary or desirable to the Research Plan, provided that there shall be no reduction in the agreed upon level of expenditures in the initial Research Plan without the consent of at least four members of the Committee.

e. The initial Research Plan and any modifications or continuations of the Research Plan subsequently adopted by the Research Committee shall have as a priority the achievement of research goals directly related to CTI's overall product development efforts and shall provide for CTI to support stem cell research on a basis that is commercially reasonable.

f. The initial Research Plan allocates resources to specific research programs and sets objective goals (the "Initial Goals") for these programs. Prior to June 30, 1999 and each June 30 thereafter through June 30, 2001, the Research Committee shall determine the Research Plan for the following twelve month period, and set objective goals, reasonably based on the Research Plan, to be achieved during such period. For so long as the Initial Goals and any subsequently adopted goals are achieved, the Research Committee shall continue to control all stem cells research conducted at CTI and SCI and CTI shall continue to fund such research at the level called for in the Research Plan adopted by the Committee (provided such funding shall not increase by more than 25% per year without the approval of CTI). CTI may, however, at any time after September 1, 1999

i. cease funding of the neural stem cells research program or reduce the level of funding for such program below the level of funding provided for such program in the Research Plan or exercise control itself over the neural stem cells research program by accelerating the vesting of all unvested Performance-Based Incentive Options related to the achievement of all milestones, other than milestones that are, at such time, time-barred and therefore no longer achievable;

ii. cease funding of the non-neural stem cells research program or reduce the level of funding for such program below the level of funding provided for such program in the Research Plan or exercise control itself over the non-neural stem cells research program by transferring to the Scientific Founders or their assigns all intellectual property created in the non-neural

stem cell research program together with all non-neural Initial Technology (as defined below) (collectively, the "Non-Neural Technology"), as more fully provided below; or

iii. so cease or reduce the funding or exercise control itself in regard to both the neural stem cell research program and the non-neural stem cell research program by either (A) transferring the Non-Neural Technology as provided in (ii) above and accelerating the options as provided in (i) above or, at CTI's option, (B) transferring both (x) the intellectual property created in the neural stem cell program together with all neural Initial Technology (collectively, the "Neural Technology," together with the Non-Neural Technology, the "Stem Cell Technology") and (y) the Non-Neural Technology to the Scientific Founders or their assigns as more fully described below.

Initial Technology shall mean existing in-licensed technology of StemCells, Inc. on the date of this Agreement. Any transfer of Technology pursuant to this paragraph shall be provided for by CTI granting to the Scientific Founders or their assigns an exclusive license or, in the case of in-licensed technology, an exclusive sublicense, to the Technology (together with the benefits of any in-licensed technology and subject to any prior out-licenses approved by the Research Committee) in consideration of the payment to CTI of cash equal to the total funding for all research conducted in the non-neural stem cell research program (in the case of a transfer of Non-Neural Technology) or the stem cell research program generally (in regard to a transfer of Stem Cell Technology). This license will be provided for in a commercially reasonable license agreement designed to permit the continued development and commercialization of the transferred Technology. In the case of any transfer of in-licensed technology, any such transfer shall be subject to all applicable terms and conditions of the in-license. In order to give CTI an on-going interest in the successful commercialization of such technology, such license agreement will provide for a royalty to be paid to CTI at a royalty rate equal to 1% of the net sales of any product whose manufacture, use or sale would but for the grant of the license infringe on any claim in any issued patent included in the licensed Technology (other than the Initial Technology). If CTI determines to cease or reduce funding or assume control as provided in (ii) or (iii) above, CTI shall promptly notify the Scientific Founders and shall give the Scientific Founders one year from the date of such notice to arrange financing for the transactions described above. The provisions of this paragraph shall terminate on the earlier of July 1, 2005 or such time as the total funding of stem cell research conducted pursuant to the Research Plan shall have exceed $25 million, at least $15 million of which shall have been expended for non-neural stem cell research.

g. All stem cells research conducted by CTI shall be under the direction of a Director of Stem Cells Research, who shall be nominated by the Research Committee, subject to reasonable approval by CTI.

2. Award of Additional Options

a. CTI shall award Options to acquire 400,000 shares of CTI Common Stock to persons (including, if the Research Committee so determines, the Scientific Founders) designated by the Research Committee, after consultation with CTI to assure (if applicable) consistency with CTI policies regarding the granting of options to employees. All persons to whom such options are granted shall be persons determined by the Research Committee, after consultation with CTI, to be persons whom it is critically important to recruit, retain or otherwise incent for the stem cells research program described above.

3. Amendment. This Agreement may be amended at any time by a written agreement executed by CTI and the Scientific Founders.

If you agree that the foregoing represents our understanding regarding the matters described in this letter agreement, please so indicate by signing the copy of this agreement (which may be executed in more than one counterpart, each of which shall constitute a single original) and returning it to us.

Very truly yours,

CYTOTHERAPEUTICS, INC.

By: /s/ Seth Rudnick

President

READ AND AGREED:

/s/ Irving L. Weissman

Irving L. Weissman

/s/ Fred H. Gage

Fred H. Gage

CROSS LICENSE AGREEMENT
BY AND BETWEEN
CYTOTHERAPEUTICS, INC.
AND
MODEX THERAPEUTICS, S.A.

ORIGINALLY DATED AS OF JULY 10, 1996
AMENDED AND RESTATED AS OF OCTOBER 29, 1997

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* This confidential portion has been omitted and filed separately with the Commission

AMENDED AND RESTATED CROSS LICENSE AGREEMENT

This AGREEMENT, originally dated as of July 10, 1996 by and between CYTOTHERAPEUTICS, INC. ("CTI"), a Delaware corporation having its principal office at Two Richmond Square, Providence, Rhode Island 02906 and MODEX THERAPEUTIQUES, SA ("Modex"), a Swiss (Vaud) corporation having its principal office at 27 Rue du Bugnon, 1005 Lausanne is hereby amended and restated, as of October 29, 1997 (the "Restatement Date"), to read in its entirety as follows:

WHEREAS, CTI has or may obtain rights to certain technology which CTI desires to license to Modex and which Modex desires to license from CTI; and

WHEREAS, Modex has or may obtain rights to certain technology which Modex desires to license to CTI and which CTI desires to license from Modex; and

WHEREAS, Modex desires to arrange for CTI to manufacture certain products to be developed by Modex and CTI wishes to manufacture such products;

NOW, THEREFORE, CTI and Modex hereby agree as follows:

1. DEFINITIONS. The following capitalized terms shall have the meanings given below:

1.1. "Confidential Information" shall mean any and all information of or about a Party including all information relating to any technology, product, process or intellectual property of such Party (including, but not limited to, owned or licensed intellectual property rights, data, know-how, samples, technical and non-technical materials, and specifications) as well as any business plan, financial information, or other confidential commercial information of or about such other Party. Notwithstanding the foregoing, specific information shall not be considered "Confidential Information" with respect to such Party to the extent that the other Party possessing such information can demonstrate by written record or other suitable physical evidence that:

(i) such specific information was lawfully in such other Party's possession or control prior to the time such information was disclosed to such other Party by the Party to whom the information relates;

(ii) such specific information was developed by such other Party without such Party having access to the Confidential Information;

(iii) such specific information was lawfully obtained by such other Party from a third Party under no obligation of confidentiality to the Party to whom such information relates; or

(iv) such specific information was at the time it was disclosed or obtained by such other Party, or thereafter became, publicly known otherwise than through a breach by such other Party of such other Party's obligations to the Party to whom such information relates.

1.2. "CTI Field" shall mean the diagnosis, prevention and treatment of diseases, conditions and disorders which affect or involve the central nervous system, (including, without limitation, pain and any ophthalmologic, auricular (hearing) or other sensory-related disease state or condition),

1.3. "CTI Know-How" shall mean

1.3.1 CURRENT ENCAPSULATION KNOW-HOW. All Confidential Information of CTI owned by CTI or under which CTI has the right to grant licenses to Modex in the Modex Field which constitutes Encapsulation Technology as of the Restatement Date (for so long as such Confidential Information continues to be Confidential Information of CTI);

1.3.2 FUTURE ENCAPSULATION KNOW-HOW. Any future Confidential Information of CTI owned by CTI or under which CTI has the right to grant licenses to Modex in the Modex Field which constitutes Encapsulation Technology (for so long as such Confidential Information continues to be Confidential Information of CTI); and

1.3.3 CURRENT CELL LINE KNOW-HOW. Certain additional Confidential Information regarding cells and cell lines owned by CTI or under which CTI has the right to grant licenses to Modex in the Modex Field as of the Restatement Date, as more specifically described on Schedule 1.3.3 (for so long as such Confidential Information continues to be Confidential Information of CTI).

Notwithstanding any other provision of this Agreement, however, CTI Know-How as described in Section 1.3.3 or elsewhere shall not include any Confidential Information relating to stem or progenitor cells of any type; any Confidential Information of CTI's subsidiary, StemCells, Inc., or any Confidential Information of CTI acquired from StemCells, Inc. (including, without limitation, any immortalization/disimmortalization technology or technology relating to stem or progenitor cells); and any Confidential Information relating to protein discovery or vaccine research.

1.4. "CTI Licensed Product" shall mean any product (i) the manufacture, use or sale of which would, absent the license granted by Modex to CTI herein, infringe an issued patent constituting a part of the Modex Patents or any portion thereof; or (ii) the manufacture, use or sale of which makes use of all or a portion of the Modex Know-How.

1.5. "CTI Patents" shall mean

1.5.1 CURRENT PATENT PORTFOLIO. Those patents (including all additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions and renewals thereof), and patent applications (including patents issued thereon) listed on Schedule 1.5, which CTI represents and warrants to Modex constitute all patents and patent applications which, as of the Restatement Date, are owned by CTI or under which CTI has the right to grant licenses to Modex in the Modex Field other than those patents or patent applications listed as "Not Included" on Schedule 1.5A;

1.5.2 FUTURE ENCAPSULATION PATENTS. Any future patent (including all additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions and renewals thereof), or patent application (including patents issued thereon) owned by CTI or under which CTI has the right to grant licenses to Modex in the Modex Field to the extent, and only to the extent, that such patent or patent application constitutes Encapsulation Technology; and

1.5.3 PATENTS DERIVED FROM CURRENT CELL LINE KNOW-HOW. Any future patent (including all additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions and renewals thereof), or patent application (including patents issued thereon) owned by CTI or under which CTI has the right to grant licenses to Modex in the Modex Field to the extent, and only to the extent, that such patent or patent application covers the CTI Know-How described in Section 1.3.3 as of the Restatement Date.

1.6. "CTI Sublicensee" shall mean any Person to whom CTI grants a sublicense of the rights granted to CTI to pursuant to Section 2.2 hereof.

1.7. "CTI Third Party Royalty Amount" shall mean any amounts CTI may from time to time be obligated to pay in respect of the manufacture, use, sale or other disposition by Modex or its Sublicensees of Modex Licensed Products or any other third-party royalty or other similar payment payable by CTI under any license granted to CTI which CTI has sublicensed to Modex hereunder.

1.8. "CTI Technology" shall mean (i) the CTI Patents and (ii) the CTI Know-How. CTI Technology shall not include Modex Technology or Joint Technology.

1.9. "Dollar" and "$" shall mean United States dollars.

1.10. "Encapsulation Technology" shall mean the following patented and non-patented technology: devices for encapsulating cells, methods of making such devices, membrane jackets for such devices, matrix cores for such devices and methods of delivering molecules from such devices. Such technology shall not include any technology relating to the encapsulated cells themselves.

1.11. "Field" shall mean collectively the CTI Field and the Modex Field.

1.12. "First Commercial Sale" shall mean, with respect to each Licensed Product in each country, the first bona fide, arms' length sale of such Licensed Product in such country following receipt of all regulatory approvals necessary to commence regular, commercial scale sales of such Licensed Product in such country. Sales prior to receipt of all approvals necessary to commence commercial sales, such as so-called "named patient sales" and "compassionate use" sales, shall not be First Commercial Sales.

1.13. "Fully Burdened Manufacturing Cost" shall mean the actual cost of the production of a Licensed Product or other implant, which shall be comprised of the sum of (a) the cost of goods produced as determined in accordance with United States generally accepted accounting principles as consistently applied by CTI, including, but not limited to, direct labor, packaging, shipping and insurance costs, and material and product testing costs incurred in connection with the manufacture or quality control testing of Modex Licensed Products or other implants, as well as overhead and amortized capital depreciation allocated to the manufacture of Modex Licensed Products or other implants in accordance with United States generally accepted accounting principles as consistently applied by CTI, and (b) all royalties (earned or paid up) and other amounts payable to third parties under license(s) taken by CTI in connection with such Modex Licensed Products, to the extent such royalties or other amounts are not included in the CTI Third Party Royalty Amount.

1.14. "Joint Technology"--see Section 4.1.

1.15. "Licensed Products" shall mean collectively the CTI Licensed Products and the Modex Licensed Products.

1.16. "Modex Field" shall mean the diagnosis, prevention and treatment, through encapsulated cell therapy, of:

1.16.1 Diabetes (other than the diagnosis, prevention or treatment of diabetes utilizing encapsulated primary islet cells);

1.16.2 Obesity;

1.16.3 Anemia;

1.16.4 The treatment of Hemophilia A or B through the delivery of Factor VIII, Factor IX or both; and

1.16.5 Two additional fields categories to be agreed to by CTI and Modex no later than June 30, 2003, each such field category to be specified by reference to a disease state or disorder and, if applicable, the delivery of a specific substance or substances. Each of the additional field categories shall be specified by Modex, subject to the consent of CTI, which

shall not be unreasonably withheld (with the withholding of any such consent based solely on the potential market share of such field category being deemed unreasonable), provided, however, that CTI may, in its sole discretion, withhold consent to any Field category involving the treatment of any disease state or disorder of the [******* ******* ****** ********** ******* ********** **** *** *** *************** ********* ********* ** ***** *************** ******* ***** ** ********** ** *** ******* ***** ** ********* *** ***** *** ** ******** ********** * ******** **********]

1.17. "Modex Know-How" shall mean

1.17.1 CURRENT ENCAPSULATION KNOW-HOW. All Confidential Information of Modex owned by Modex or under which Modex has the right to grant licenses to CTI in the CTI Field which constitutes Encapsulation Technology as of the Restatement Date (for so long as such Confidential Information continues to be Confidential Information of Modex);

1.17.2 FUTURE ENCAPSULATION KNOW-HOW. Any future Confidential Information of Modex owned by Modex or under which Modex has the right to grant licenses to CTI in the CTI Field which constitutes Encapsulation Technology (for so long as such Confidential Information continues to be Confidential Information of Modex); and

1.17.3 CURRENT CELL LINE KNOW-HOW. Certain additional Confidential Information regarding cells and cell lines owned by Modex or under which Modex has the right to grant licenses to CTI in the CTI Field as of the Restatement Date, as more specifically described on Schedule 1.17.3 (for so long as such Confidential Information continues to be Confidential Information of Modex).

1.18. "Modex Licensed Products" shall mean any product (i) the manufacture, use or sale of which would, absent the license granted by CTI to Modex herein, infringe an issued patent constituting a part of the CTI Patents, or any portion thereof, or (ii) the manufacture, use or sale of which makes use of all or a portion of the CTI Know-How.

1.19. "Modex Patents" shall mean

1.19.1 CURRENT PATENT PORTFOLIO. Those patents (including all additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions and renewals thereof), and patent applications (including patents issued thereon) listed on Schedule 1.19, which Modex represents and warrants to CTI constitute all patents and patent applications which, as of the Restatement Date, are owned by Modex or under which Modex has the right to grant licenses to CTI in the CTI Field other than those patents or patent applications listed as "Not Included" on Schedule 1.19A;

1.19.2 FUTURE ENCAPSULATION PATENTS. Any future patent (including all additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term

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* This confidential portion has been omitted and filed separately with the Commission

extensions and renewals thereof), or patent application (including patents issued thereon) owned by Modex or under which Modex has the right to grant licenses to CTI in the CTI Field to the extent, and only to the extent, that such patent or patent application constitutes Encapsulation Technology; and

1.19.3 PATENTS DERIVED FROM CURRENT CELL LINE KNOW-HOW. Any future patent (including all additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions and renewals thereof), or patent application (including patents issued thereon) owned by Modex or under which Modex has the right to grant licenses to CTI in the CTI Field to the extent, and only to the extent, that such patent or patent application covers the Modex Know-How described in Section 1.17.3 as of the Restatement Date.

1.20. "Modex Technology" shall mean (i) the Modex Patents, and (ii) the Modex Know-How. Modex Technology shall not include CTI Technology or Joint Technology.

1.21. "Modex Sublicensee" shall mean any Person to whom Modex grants a sublicense of the rights granted to Modex pursuant to Section 2.1 hereof.

1.22. "Modex Third Party Royalty Amount" shall mean any amounts Modex may from time to time be obligated to pay in respect of the manufacture, use, sale or other disposition by CTI or its Sublicensees of the CTI Licensed Products or any other third-party royalty or other similar payment payable by Modex under any license granted to Modex which Modex has sublicensed to CTI hereunder.

1.23. "Net Sales" shall mean as to any period for each Licensed Product in a given country, the gross invoiced sales price for all such Licensed Products sold or commercially disposed of for value in such country by a Party, or such Party's Sublicensees, in arm's length sales to independent third parties in that period, after deduction of the following items incurred by a Party or such Party's Sublicensees, as the case may be, during such period with respect to sales of Licensed Products hereunder regardless of the period in which such sales were made, provided that such items are included in the price charged, and do not exceed reasonable and customary amounts in the country in which such sale occurred:

(i) trade and quantity discounts or rebates actually taken or allowed;

(ii) credits or allowances given or made for rejection or return of previously sold Licensed Products actually taken or allowed;

(iii) any tax or government charge (including any tax such as a value added or similar tax or government charge other than an income tax) levied on the sale, transportation or delivery of a Licensed Product and borne by the seller thereof; and

(iv) any charges for freight or insurance billed to the final customer.

If a Licensed Product is sold, leased or otherwise commercially disposed of for value (including, without limitation, disposition in connection with the delivery of other products or services) in a transaction that is not an arm's length transaction with an independent third Party, and is not for resale, etc. to an independent Party in an arm's length transaction, then the gross sales price in such transaction shall be deemed to be the greater of the actual sales price or the gross sales price in the most similar substantially contemporaneous arm's length sale to an independent third Party for such Licensed Product, or if there is none, for the most similar Licensed Product for which there is a transaction. Net Sales shall also include any other consideration received by a Party or its Sublicensees in respect of the sale, distribution or transfer of a Licensed Product other than in the course of clinical trials.

1.24. "Party" shall mean each of CTI and Modex and their respective successors and permitted assigns.

1.25. "Person" shall mean any person, entity, organization or body.

1.26. "Sublicensees" shall mean collectively the CTI Sublicensees and the Modex Sublicensees.

2. LICENSE TERMS

2.1. LICENSE GRANT TO MODEX. Subject to the terms and conditions of this Agreement, CTI hereby grants to Modex an exclusive, royalty-bearing, worldwide license, including the right to grant sublicenses, under the CTI Technology to use, sell and have sold Modex Licensed Products in the Modex Field.

2.1.1 MANUFACTURING LICENSE UNDER CTI PATENTS. Subject to the terms and conditions of this Agreement (including, without limitation, the provisions of Section 6.6), CTI also hereby grants to Modex a co-exclusive, royalty-bearing world-wide license, including the right to grant sublicenses, under the CTI Patents, to manufacture and to have manufactured Modex Licensed Products in the Modex Field.

2.1.2 MANUFACTURING LICENSE UNDER CTI KNOW-HOW. Subject to the terms and conditions of this Agreement (including, without limitation, the provisions of Section 6.6), CTI also hereby grants to Modex a Non-exclusive, royalty-bearing world-wide license, including the right to grant sublicenses, under the CTI Know-How, to manufacture and to have manufactured Modex Licensed Products in the Modex Field.

2.2. LICENSE GRANT TO CTI. Subject to the terms and conditions of this Agreement, Modex hereby grants to CTI (i) a non-exclusive, royalty-free, worldwide license, including the

right to grant sublicenses, under the Modex Technology to manufacture, and have manufactured, the Modex Licensed Products, and (ii) an exclusive, royalty-bearing, worldwide license, including the right to grant sublicenses, under the Modex Technology to manufacture, have manufactured, use, sell and have sold CTI Licensed Products in the CTI Field.

2.3. LIMITED RIGHTS. The rights granted hereunder shall be limited to the rights expressly stated to be granted hereunder and no additional right or licenses are implied. Without limiting the generality of the foregoing, nothing in this Agreement shall be construed to grant (i) to Modex rights under any CTI Technology to make, have made, use, sell or have sold any products other than the Modex Licensed Products in the Modex Field or (ii) to CTI (A) rights under any Modex Technology to make or have made any products other than the Modex Licensed Products or (B) rights under any Modex Technology to make, have made, use, sell or have sold any products other than the CTI Licensed Products in the CTI Field, except as provided in (A) above.

2.4. JOINT TECHNOLOGY. Subject to the provisions of this Section 2.4, each Party shall have the right to exploit the Joint Technology without being obligated to account to the other Party.

2.4.1 MODEX LICENSE TO JOINT TECHNOLOGY. In the event during the term of this Agreement Modex desires to obtain exclusive rights to the Joint Technology to make, have made, use, sell and have sold products in the Modex Field, Modex shall give notice to CTI of its desire and this Agreement shall be appropriately modified to give Modex such rights and to include such products in the definition of Modex Licensed Products, which CTI or Modex shall manufacture or have manufactured as provided in Section 6, and which shall entitle CTI to receive royalty payments equal to the Specified Percentage of the Net Sales of such products as provided in Section 3.

2.4.2 CTI LICENSE TO JOINT TECHNOLOGY. In the event during the term of this Agreement CTI desires to obtain exclusive rights to the Joint Technology to make, have made, use, sell and have sold products in the CTI Field, CTI shall give notice to Modex of its desire and this Agreement shall be appropriately modified to give CTI such rights and to include such products in the definition of CTI Licensed Products, which shall entitle Modex to receive royalty payments equal to [*** ******* ****] of the Net Sales of such products as provided in Section 3.

2.5. SUBLICENSEES. Each Party shall give notice to the other of any Sublicensee appointed by it. The Party appointing a Sublicensee shall be responsible for all obligations of such Sublicensee hereunder, including without limitation their obligation to pay royalties on sales of Licensed Products, and the obligation of such Sublicensees not to sell Licensed Products outside, in the case of Modex Sublicensees, the Modex Field, and, in the case of CTI Sublicensees, the CTI Field. In the event that the license granted to Modex hereunder by CTI shall terminate for any reason, any Sublicensee under any such terminated license shall

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* This confidential portion has been omitted and filed separately with the Commission

continue automatically to have the rights and license previously licensed by CTI to Modex under such terminated license and shall be entitled to enforce such rights and license directly against CTI, provided that any such Sublicensee agrees in writing with CTI that CTI shall be entitled to enforce the provisions of such terminated license directly against such Sublicensee. In the event that the license granted to CTI hereunder by Modex shall terminate for any reason, any Sublicensee under any such terminated license shall continue automatically to have the rights and license previously licensed by Modex to CTI under such terminated license and shall be entitled to enforce such rights and license directly against Modex, provided that any such Sublicensee agrees in writing with Modex that Modex shall be entitled to enforce the provisions of such terminated license directly against such Sublicensee. At the request of either Party, the other Party shall enter into a direct contractual arrangement with any Sublicensee of the requesting Party providing for such Sublicensee to have such rights and obligations as described in the two preceding sentences, effective upon any termination of the license granted hereunder from the requested Party to the requesting Party.

2.6. TECHNOLOGY TRANSFER. Each Party shall, at its own expense, provide the other Party with reasonable cooperation in order to permit each such Party to exploit the rights granted to it hereunder.

3. ROYALTIES

3.1. ROYALTIES PAYABLE BY MODEX. Except as otherwise provided herein, following the First Commercial Sale of each Modex Licensed Product, Modex shall pay to CTI a royalty equal to (i) the Specified Percentage of Net Sales for such Modex Licensed Product in each calendar quarter, plus (ii) any CTI Third Party Royalty Amount payable in respect of such Modex Licensed Products. The royalty payable shall be calculated separately for each country and for each Modex Licensed Product. Modex shall be responsible for the payment of, and shall remit to CTI, all royalties payable to CTI hereunder. No multiple royalties shall be payable because the manufacture, use or sale of any Modex Licensed Product (i) shall be covered by more than one CTI Patent and/or any patent included in Joint Technology or (ii) uses or incorporates more than one aspect of the CTI Technology and/or Joint Technology or both (i) and (ii) apply. The Specified Percentage shall equal [*** ******* ****], except as otherwise provided in Section 6.6.

3.2. ROYALTIES PAYABLE BY CTI. Except as otherwise provided herein, following the First Commercial Sale of each CTI Licensed Product, CTI shall pay to Modex a royalty equal to (i) [*** ******* ****] of Net Sales for such CTI Licensed Product in each calendar quarter, plus (ii) the Modex Third Party Royalty Amount payable in respect of such CTI Licensed Products. The royalty payable shall be calculated separately for each country and for each CTI Licensed Product. CTI shall be responsible for the payment of, and shall remit to Modex, all royalties payable to Modex hereunder. No multiple royalties shall be payable because the manufacture, use or sale of any CTI Licensed Product (i) shall be covered by more than one

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Modex Patent and/or any patent included in Joint Technology or (ii) uses or incorporates more than one aspect of the Modex Technology and/or Joint Technology or both (i) and (ii) apply.

3.3. TERMINATION OF ROYALTY OBLIGATIONS. With respect to each Licensed Product, the royalty obligations of each of Modex and CTI shall cease upon the later of (i) the last to expire of any patent which would be infringed by the manufacture, use or sale of such Licensed Product but for a license granted hereunder; (ii) on a country-by-country basis, the date that is ten (10) years from the First Commercial Sale in any country of such Licensed Product; and (iii) with respect to any CTI Third Party Royalty Amount or Modex Third Party Royalty Amount, the expiration of the obligation of, respectively, CTI or Modex to pay any such amount.

3.4. PAYMENT DATES AND STATEMENTS. Within forty-five (45) days of the end of each calendar quarter in which Net Sales occur, each Party shall calculate the royalty amount owed under this Section 3 and shall remit such amount to the other Party. Such payment shall be accompanied by a statement showing the calculation of the amount owed for each country, the total Net Sales of each Licensed Product by country for that quarter, and the exchange rate (as determined pursuant to Section 3.6) used to directly convert any royalty amounts into Dollars. For purposes of determining when a sale of a Licensed Product occurs, the sale shall be deemed to occur on the earlier of: (i) the date the Licensed Product is shipped by CTI or Modex, as applicable, or (ii) the date of the invoice to the purchaser of the Licensed Product. Any payment owed under this Section 3 that is not paid on or before the date such payment is due under this Agreement shall bear interest, to the extent permitted by applicable law, at two percentage points (2%) over the prime rate of interest as reported in the New York edition of The Wall Street Journal on the due date of such payment calculated on the number of days such payment is delinquent. If materially different from the foregoing provisions, any CTI Third Party Royalty Amount or Modex Third Party Royalty Amount shall be calculated and paid in accordance with the provisions applicable to the payment of any such amount.

3.5. RECORDS AND ACCOUNTING. Each Party shall keep, and shall cause its Sublicensees to keep, complete and accurate records of the latest three (3) years of its Net Sales. Each Party shall have the right annually at its own expense to have an independent, certified public accountant to which the other Party has no reasonable objection, review such records upon reasonable notice and during reasonable business hours for the purposes of verifying royalties payable to it hereunder and Net Sales by the other Party and its Sublicensees. Results of such review shall be made available to both parties. If the review reflects an underpayment of royalties, such underpayment shall be promptly remitted to the Party to whom such royalties are payable with interest as provided in Section 3.4. If the underpayment is equal to or greater than five percent (5%) of the royalty amount that was otherwise due, the Party to whom such royalties are payable shall be entitled to have the other Party pay all of the costs of such review. Each Party shall cause its accountant undertaking a review of the other Party's records pursuant to this Section 3.5 to treat all information of such Party's records as Confidential Information of such Party and such accountant shall disclose to

its client only such information as is relevant to determining the accuracy of the royalties paid. Each party shall also maintain such records and take such other actions as the other party may reasonably require in connection with the determination of any CTI Third Party Royalty Amount or Modex Third Party Royalty Amount.

3.6. CURRENCY OF PAYMENTS. All payments under this Agreement shall be made in Dollars by wire transfer to such bank account as the Party to whom royalties are payable may designate from time to time. Any payments due hereunder on Net Sales outside of the United States shall be payable in Dollars at the rate of exchange of the currency of the country in which the Net Sales are made as reported in the New York edition of The Wall Street Journal for the last business day of the quarter for which the royalties are payable. Where royalties are due hereunder for Net Sales in a country where, by reason of currency regulations or taxes of any kind, it is illegal for the Party obligated to transfer royalty payments out of such country for Net Sales in that country, such royalties shall be deposited in a currency that is permitted for the Party not able to make the transfer for the benefit or credit of the other Party. If materially different from the foregoing provisions, any CTI Third Party Royalty Amount or Modex Third Party Royalty Amount shall be calculated and paid in accordance with the provisions applicable to the payment of any such amount.

3.7. TAX WITHHOLDING. Modex and CTI shall use all reasonable and legal efforts to reduce tax withholding on payments made hereunder. Notwithstanding such efforts, if the Parties conclude that tax withholdings are required with respect to payments made hereunder, the Party making such payments shall withhold the required amount and pay it to the appropriate governmental authority. In such a case, the Party paying such amount will promptly provide the other Party with original receipts or other evidence sufficient to allow the other Party to obtain the benefits of such tax withholdings. If materially different from the foregoing provisions, any tax withholding with respect to any CTI Third Party Royalty Amount or Modex Third Party Royalty Amount shall be governed by the provisions applicable to tax withholding with regard to such amount.

4. PATENTS AND TECHNOLOGY

4.1. OWNERSHIP OF TECHNOLOGY. Each Party shall retain sole title to any technology which it develops solely. Except as provided in this Agreement, neither Party shall have any right to use or license technology to which the other Party has sole title. Each Party shall own a fifty percent (50%) undivided interest in all technology, know-how, inventions, concepts, processes and the like (whether or not patentable) made, conceived, reduced to practice or generated jointly by or on behalf of both parties ("Joint Technology").

4.2. JOINT PATENTS. CTI shall prepare, file and prosecute patent applications, covering any Joint Technology in the countries of CTI's choice (after consultation with Modex) with appropriate credit to Modex, including naming representatives of Modex as inventors where appropriate. CTI and Modex shall share equally all of the costs associated with the

preparation, filing and prosecution of such patent applications in such countries. The Parties shall assist each other to the maximum extent reasonable in securing intellectual property rights resulting from their respective research programs. Either Party may withdraw from or abandon any jointly-owned patent or patent application on notice to the other in which case any such patent or patent application shall become the sole property of the other Party. If Modex wishes to prepare, file or prosecute any patent application covering any Joint Technology in a country where CTI, after consultation with Modex, determines not to file such application, Modex may do so after reasonable notice to CTI, in which case CTI shall either share equally all of the costs associated with the preparation, filing and prosecution of such patent application in such country or such patent application and any patent or patents that may issue therefrom shall become the sole property of Modex.

4.3. INFRINGEMENT OF PATENTS. If a Party has reason to believe that any of the patents of the other is being infringed by a third party, the former shall promptly notify the latter and shall provide it with any evidence of any infringement which is reasonably available. The Party owning such patent shall have the first opportunity at its own expense to attempt to resolve such infringement by appropriate steps including suit. In such event, the other Party will assist in taking such steps, including suit, within reasonable limits, and any amount recovered as a result thereof shall first be applied to reimbursing the Party taking such action for its out-of-pocket expenses, then for reimbursing the other Party for its out-of-pocket expenses incurred in connection with such action, and the remainder, if any, shall be for the account of the Party owning such patent. In the event the Party owning such patent fails to cause such infringement to cease or institute suit or other legal action with respect to any such infringement within a period of six (6) months following such notice of infringement, the other Party shall have the right to take any appropriate steps, including filing suit against the infringer at its own expense and in the name of the Party owning the patent, if necessary. In such event, the other Party shall assist the Party bringing suit as reasonably requested and shall permit the Party bringing suit to prosecute such infringement in the name of the owner of the patent. The expenses reasonably incurred in taking such steps, including suit and legal action, and any amount recovered as a result thereof shall be first applied to reimbursing the Party taking such action for out-of-pocket expenses, and then to reimbursing the Party not taking such action for its out-of-pocket expenses incurred in connection with such action, and the remainder, if any, shall be for the account of the Party taking such action.

4.4. SURVIVAL. This Section 4 shall survive the termination or expiration of this Agreement.

5. CONFIDENTIAL INFORMATION

5.1. TREATMENT OF CONFIDENTIAL INFORMATION. Each Party hereto shall maintain the Confidential Information of the other Party in confidence, and shall not disclose, divulge or otherwise communicate such Confidential Information to others, or use it for any purpose, except pursuant to, and in order to carry out, the terms and objectives of this Agreement, and

each Party hereby agrees to exercise every reasonable precaution to prevent and restrain the unauthorized disclosure of such Confidential Information by any of its directors, officers, employees, consultants, subcontractors, Sublicensees or agents.

5.2. RELEASE FROM RESTRICTIONS. The provisions of Section 5.1 shall not apply to any Confidential Information disclosed hereunder which is: required to be disclosed by the receiving Party to comply with applicable laws, or to comply with laws or regulations (including without limitation testing and marketing regulations), in each case only to the extent required to carry out the work contemplated by this Agreement or other legal obligations provided that the receiving Party provides prior written notice of such disclosure to the other Party and takes reasonable and lawful actions to avoid and/or minimize the degree of such disclosure.

5.3. CONFIDENTIAL AGREEMENTS. Each Party shall maintain employment agreements with their respective employees and representatives providing for confidentiality and nonuse commitments consistent with its obligations hereunder and will require all of its employees, consultants, agents or others who have access to any Confidential Information of the other Party to execute confidentiality agreements covering all Confidential Information subject to Section 5 and will exercise its reasonable best efforts to obtain compliance therewith.

6. SUPPLY OF MODEX LICENSED PRODUCT

6.1. GENERAL. Except as provided in Section 6.6, CTI shall exclusively manufacture or have manufactured and supply all Modex Licensed Products for Modex and all Modex Sublicensees, as well as any other implants (e.g., placebos or other controls) deemed necessary or desirable by Modex or any Modex Sublicensee in connection with the development or clinical trials of any Modex Licensed Product, and Modex and any Modex Sublicensee shall exclusively rely on CTI to so manufacture or have manufactured all Modex Licensed Products, all as more fully provided below.

6.2. SUPPLY OF MODEX LICENSED PRODUCTS FOR CLINICAL TRIALS. The transfer price to Modex of all Modex Licensed Products and other implants used in clinical trails of any Modex Licensed Product or any pre-clinical research regarding any such product shall be [**** ** ***** ***** ******** ********** ****] of such Modex Licensed Products and implants. CTI shall not be required to supply more than 10 implants per Modex Licensed Product in any week through the completion of Phase II clinical trials or more than 25 implants per week per Modex Licensed Product during Phase III clinical trials (including named patient sales). Modex shall provide CTI with reasonable lead time to manufacture all such Modex Licensed Products and other implants for clinical trial use. If Modex requires greater quantities of implants for any clinical trial for any Modex Licensed Product, Modex will give CTI ninety (90) days prior notice and CTI will use commercially reasonable efforts to accommodate such request.

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* This confidential portion has been omitted and filed separately with the Commission

6.3. SUPPLY OF MODEX LICENSED PRODUCTS FOR COMMERCIAL SALE.

6.3.1 TRANSFER PRICE. The transfer price for all Modex Licensed Products other than those used in clinical trials shall be calculated in accordance with the following formula (the "Commercial Transfer Price"):

CTP = [*** ****** ** *** *** *** ****** ** **** **** ** ****]

Where: CTP = Commercial Transfer Price

FBMC = CTI's Fully Burdened Manufacturing Cost of such Modex Licensed Product

Cap Amount = [*** ******* ** *** **** *** ******** **** ****** ** ** ******** ** ***** **** **** ** **** **** ** ******* *** ******** ** *** ******** ***** ***** ***** ********** ** ********* ** *** ****** ** ***** ********** ** *** ****** ****** ********** ** ****** ** **** **** ** ****].

The following examples indicate the application of this formula:

[**********	**** ** ****	****	**** ** ****	***
****	****	****	****	
****	****	****	****	
****	****	****	****	
****	****	*******	****	
****	****	*******	*****	

6.3.2 ESTIMATE OF NEED FOR MODEX LICENSED PRODUCT. At least two (2) years before the expected first launch of any Modex Licensed Product in any country, Modex shall inform CTI of its best estimate of the quantity of such Modex Licensed Product needed by Modex for use or sale during the initial two (2) years after launch. Such estimates will thereafter be updated annually.

To assist CTI in preparing for its supply of Modex Licensed Product, Modex will provide CTI with the following signals for each Licensed Product:

SIGNAL	TIMING	FORECAST
1	Prior to Phase II studies	Market potential estimates based on market research.

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SIGNAL	TIMING	FORECAST
2	Prior to Phase III studies	Market potential estimates based on more comprehensive market research, targeted indications or suggested by Phase II data.
3	Prior to 1st Product License Application or equivalent to the US Food and Drug Administration (the "FDA") or similar foreign filing (1-1 1/2yrs before launch)	Final pre-launch forecast based on extensive market research using Phase III results and considering reimbursement issues.

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The estimates given by Modex pursuant to this Paragraph 6.3.2 will be used by CTI only for the purpose of preparing CTI's production capacity for Modex Licensed Product.

6.3.3 QUARTERLY FORECAST. Starting twelve (12) months prior to the expected first launch of any Modex Licensed Product, Modex will, before each January 1, April 1, July 1 and October 1, present to CTI a written forecast estimating the monthly quantities of Modex Licensed Products to be delivered during the next twelve (12) month period. With such forecast, Modex will provide CTI with a summary of its inventory, if any.

Modex will place firm orders for delivery not less than ninety (90) days prior to the start of the calendar quarter for which shipment is ordered, and CTI will be obliged (subject to such orders being within CTI's supply capacity, assuming proportional allocation of such capacity based on firm orders for such capacity) to deliver all ordered quantities of Modex Licensed Product by the delivery date stated in the order, except to the extent that such quantities would exceed either of the following:

(a) 130% of the twelve (12) months forecast for such quarter made twelve (12) months prior to the start of such quarter; and

(b) 120% of the six (6) months forecast for such quarter made six (6) months prior to the start of such quarter.

Similarly, the quantities subject to such firm order shall not be less than either of the following:

(c) 70% of the twelve (12) months forecast for such quarter made twelve (12) months prior to the start of such quarter; and

(d) 80% of the six (6) months forecast for such quarter made six (6) months prior to the start of such quarter.

In addition, the firm order for any quarter shall not require delivery of more than forty percent (40%) of such order in any one month.

CTI will, however, make reasonable efforts also to supply quantities of Modex Licensed Product in excess of forecast amounts if ordered by Modex.

6.3.4 PAYMENT AND DELIVERY TERMS. Each delivery of Modex Licensed Product will be effected ex works (CTI's plant) (Incoterms 1990 as published by the International Chamber of Commerce). All quantities of Modex Licensed Product will be delivered in finished form, ready for sale and suitably packed for transportation. Payment for Modex Licensed Products shall be made within 30 days following delivery.

6.3.5 CIRCUMSTANCES AFFECTING SUPPLY. Each Party will promptly notify the other Party of any circumstances that it believes may be of importance as to CTI's ability to supply Modex with Modex Licensed Product.

6.4. SPECIFICATIONS. All Modex Licensed Products manufactured by CTI pursuant to this Agreement shall, upon delivery to Modex, conform to the specifications for such Modex Licensed Product to be agreed upon by Modex and CTI.

6.5. ADDITIONAL MANUFACTURING FACILITY. If prior to the termination of Modex' rights and licenses hereunder, the parties determine that CTI will be required to construct an additional facility to meet the demand for the supply of Modex Licensed Products, CTI agrees to use reasonable efforts to locate such facility in Switzerland. CTI's obligation to use reasonable efforts to construct such facility in Switzerland is subject to CTI's determination that such facility would be commercially practicable in light of the demand for CTI's other products and the agreement by the Parties on minimum purchase obligations on the part of Modex that would make such facility profitable. CTI would be permitted to utilize any such facility for the manufacture of products other than Modex Licensed Products.

6.6. EXERCISE BY MODEX OF RIGHTS TO MANUFACTURE OR HAVE MANUFACTURED MODEX LICENSED PRODUCTS.Modex may exercise its rights to manufacture or have manufactured Modex Licensed Products pursuant to the licenses granted by CTI to Modex under Sections 2.1.1 and 2.1.2 on the following terms and conditions:

6.6.1 CTI'S FAILURE TO PERFORM. If CTI fails to supply Modex or any Modex Sublicensee as required under the preceding provisions of this Section 6, following written notice from Modex and a commercially reasonable opportunity to cure, Modex may exercise its rights under the licenses granted to Modex under Sections 2.1.1 and 2.1.2, and the Specified Percentage shall remain [*** ******* ****]. CTI shall maintain at all times

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* This confidential portion has been omitted and filed separately with the Commission

sufficiently detailed records of the CTI Know-How required for the manufacture of Modex Licensed Products so as to allow Modex to exercise its license rights to such CTI Know-How if CTI fails to perform for any reason, including, without limitation, CTI's bankruptcy or insolvency.

6.6.2 MODEX'S DECISION TO MANUFACTURE. Modex may at any time exercise its rights under the license granted to it by CTI under Section 2.1.1 by providing CTI with 90 days advance written notice of its intention to so manufacture or have manufactured Modex Licensed Products. The Specified Percentage in regard to the Net Sales of any Modex Licensed Product which Modex manufactures or has manufactured pursuant to the provisions of this Section 6.6.2 shall be [***** ******* ****]. The exercise by Modex of its rights under this Section 6.6.2 shall not relieve Modex of its obligations with respect to any firm order placed under Section 6.3. The Parties intend that Modex may exercise its rights under this Section 6.6.2 with respect to a portion of the manufacture of any Modex Licensed Product or with respect to certain Modex Licensed Products but not others.

6.6.3 MODEX'S RIGHTS TO MANUFACTURE WHERE TRANSFER PRICE EXCEEDS [***] OF NET SALES. In the event that [***] of the aggregate Net Sales of any type of Modex Licensed Product in any calendar quarter is less than the aggregate Commercial Transfer Price payable with respect to the delivery of Modex Licensed Products, Modex may so notify CTI, in which event, CTI shall either reduce the aggregate Commercial Transfer Price payable with respect to such Modex Licensed Products to no more than [***] of such aggregate Net Sales or (ii) permit Modex to exercise its rights under Section 2.1.1, in which case the Specified Percentage in regard to Net Sales of such Modex Licensed Product shall be [**** ******* ****] rather than [***** ******* ****].

7. TERM AND TERMINATION

7.1. TERM. The term of this Agreement (the "Term") shall commence as of the Effective Date. Unless sooner terminated pursuant to Section 7.2 or 7.3, the term of this Agreement shall expire at such time as neither Party shall have any further obligations to pay royalties on the sale of Licensed Products.

7.2. BREACH. Failure by a Party to comply with any of its material obligations contained in this Agreement shall entitle the other Party to give to the Party in default notice specifying the nature of the default and requiring it to cure such default. If such default is not cured within 30 days after the receipt of such notice (or 90 days in the event such breach cannot be reasonably expected to be cured within 30 days, and the defaulting Party gives notice to the other Party of its inability to cure such default within a 30 day period and the defaulting Party thereafter uses reasonable efforts to cure such default as soon as practicable), the notifying Party shall be entitled, without prejudice to any of its other rights under this Agreement, and in addition to any other remedies available to it by law or in equity, to terminate the rights and licenses of the defaulting Party under this Agreement by giving notice

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* This confidential portion has been omitted and filed separately with the Commission

to that effect to the defaulting Party. The right of either Party to terminate the rights and licenses granted to the other Party under this Agreements as hereinabove provided shall not be affected in any way by its waiver or failure to take action with respect to any previous default.

7.3. INSOLVENCY OR BANKRUPTCY. Either Party may, in addition to any other remedies available to it by law or in equity, terminate the rights and licenses granted to the other Party under this Agreement by written notice to the other Party in the event (i) the other Party shall have become insolvent or bankrupt, or shall have made an assignment for the benefit of its creditors, or (ii) there shall have been appointed a trustee or receiver of the other Party or for all or a substantial part of its property, or (iii) any case or proceeding shall have been commenced or some other action taken by or against the other Party in bankruptcy or seeking reorganization, liquidation, dissolution, winding-up, arrangement, composition or readjustment of its debts or any other relief under any bankruptcy, insolvency, reorganization or other similar act or law of any jurisdiction now or hereafter in effect or there shall have been issued a warrant of attachment, execution, distraint or similar process against any substantial part of the property of the other Party, and any such event or action shall have continued for 60 days undismissed, unbounded and undischarged; provided, however, that no such right to terminate shall pertain solely by virtue of a voluntary reorganization for the purpose of solvent amalgamation or reconstruction. To the extent that the provisions of any bankruptcy or insolvency law applicable to the bankruptcy or insolvency of Modex fail to provide CTI as Licensee of Modex hereunder with rights analogous to those which Modex enjoys under the provisions of United States bankruptcy law in regard to its ability to continue to exercise its rights under the licenses granted to Modex by CTI hereunder so long as Modex continues to satisfy its obligations hereunder, appropriate provisions will be added to this Agreement providing CTI, to the maximum extent possible, with such analogous rights.

7.4. EFFECT OF TERMINATION.

(a) Upon termination of this Agreement for any reason, nothing herein shall be construed to release either Party from any obligation that matured prior to the effective date of such termination.

(b) The termination pursuant to Sections 7.2 or 7.3 of the rights and licenses granted to a Party under this Agreement shall not affect the rights and licenses of the other Party under this Agreement, provided such other Party continues to comply with its obligations hereunder.

(c) Upon the termination of a Party's rights and licenses granted under this Agreement for any reason, the terminated Party shall return and deliver to the other Party all materials and documents developed during the performance of this Agreement, all data and records required by the FDA or other regulatory authorities to be maintained with respect to the sale, storage, handling, shipping and use of the Licensed Products of the other Party, all reimbursement approval

files, all documents, data and information related to clinical trials and other studies of Licensed Products of the other Party required by the FDA or other regulatory authorities, and all copies and facsimiles of such materials, documents, information and files. Such other Party shall have the right to utilize and allow others to utilize all such materials, documents and records in connection with the development, regulatory approval, manufacture and sale of its Licensed Products and the terminated Party shall provide such other Party with reasonable cooperation, including without limitation, providing such other Party with a letter authorizing such other Party to cross reference the terminated Party's files with the FDA or other regulatory body.

(d) The provisions of Sections 4 (Patents and Technology), 5 (Confidential Information), 8.11 (Modex Indemnification), 8.12 (CTI Indemnification), 8.13 (Liability Insurance) and 9 (Resolution of Disputes) shall survive termination of this Agreement or termination of any Party's rights and licenses for any reason. Provided the rights and licenses granted to a Party under this Agreement have not been previously terminated, upon expiration of the Term of this Agreement, the licenses granted to such Party hereunder shall become nonexclusive and royalty free.

8. MISCELLANEOUS PROVISIONS

8.1. NO PARTNERSHIP. Nothing in this Agreement is intended or shall be deemed to constitute a partnership, agency, employer, employee or joint venture relationship between the Parties. Neither Party shall incur any debts or make any commitments for the other.

8.2. ASSIGNMENTS. Except as otherwise provided herein, neither this Agreement nor any interest hereunder shall be assignable by either Party by operation of law or otherwise without the prior written consent of the other; provided, however, that either Party may assign this Agreement to any wholly-owned subsidiary or to any successor by merger or sale of substantially all of its assets to which this Agreement relates in a manner such that the assignor shall remain liable and responsible for the performance and observance of all its duties and obligations hereunder, or if the assignor disappears because of such transaction, the assignee must agree to abide by the terms and conditions of this Agreement. This Agreement shall be binding upon the successors and permitted assigns of the parties.

8.3. FORCE MAJEURE. Neither Party shall be liable to the other for loss or damages or shall have any right to terminate this Agreement for any default or delay (including, without limitation, an inability to supply Licensed Product) attributable to any act of God, earthquake, flood, fire, explosion, strike, lockout, labor dispute, casualty or accident, war, revolution, civil commotion, act of public enemies, blockage or embargo, injunction, law, order, proclamation, regulation, ordinance, demand or requirement of any government or subdivision, authority (including, without limitation, drug regulatory authorities) or

representative of any such government, or any other cause beyond the reasonable control of such Party, if the Party affected shall give prompt notice of the commencement and cessation of any such cause to the other Party. The Party given such notice shall thereupon be excused from such of its obligations hereunder as it is so disabled and for 30 days thereafter. Notwithstanding the foregoing, nothing in this Section shall excuse or suspend the obligation to make any payment due hereunder in the manner and at the time provided.

8.4. NO TRADEMARK RIGHTS. No right, express or implied, is granted by this Agreement to use in any manner any trade name or trademark of CTI or Modex in connection with the performance of this Agreement or the exploitation of any license granted hereunder.

8.5. PUBLIC ANNOUNCEMENTS. Except as required by law or the rules of any exchange or quotation system on which a Party's capital stock is then traded or listed, neither Party will issue any press release or make any public announcement of the existence or terms of this Agreement without prior consultation with and approval by the other Party, which consent shall not be unreasonably withheld or delayed.

8.6. ENTIRE AGREEMENT OF THE PARTIES; AMENDMENT. This Agreement constitutes and contains the entire understanding and agreement of the Parties and cancels and supersedes any and all prior negotiations, correspondence and understandings and agreements, whether verbal or written, between the Parties respecting the subject matter hereof. No waiver, modification or amendment of any provision of this Agreement shall be valid or effective unless made in writing and signed by a duly authorized officer of each of the Parties.

8.7. SEVERABILITY. In the event any one or more of the provisions of this Agreement should for any reason be held by any court or authority having jurisdiction over this Agreement or either of the Parties to be invalid, illegal or unenforceable, such provision or provisions shall be validly reformed by addition or deletion of wording as appropriate to avoid such result and as nearly as possible approximate the intent of the Parties and, if unreformable, shall be divisible and deleted in such jurisdiction; elsewhere, this Agreement shall not be affected.

8.8. CAPTIONS. The captions to this Agreement are for convenience only, and are to be of no force or effect in construing or interpreting any of the provisions of this Agreement.

8.9. NOTICE AND DELIVERY. Any notice, request, delivery, approval or consent required or permitted to be given under this Agreement shall be in writing and shall be deemed to have been sufficiently given if delivered in person, transmitted by internationally recognized courier, telegraph or telecopier (with confirmed answer-back) or sent by registered air mail letter to the Party (which notice shall be considered effective five days after it is sent) to whom it is directed at its address shown below or such other address as such Party shall have last given by notice to the other Party.

If to CTI, addressed to: CytoTherapeutics, Inc.
Two Richmond Square
Providence, Rhode Island 02906
Attention: Vice President, Business Development
Telephone: (401) 272-3310
Telecopier: (401) 272-3485
with a copy addressed to the General Counsel

If to Modex, addressed to: Modex Therapeutiques, SA
Rue de Bugnon, 27
1005 Lausanne
Switzerland
Attention: Managing Director
Telephone: 011-41-21-692-5450
Telecopier: 011-41-21-692-5455

8.10. LIMITATION OF LIABILITY. Neither Party shall be liable to the other for indirect, incidental or consequential damages arising out of any of the terms or conditions of this Agreement or with respect to their performance or lack thereof.

8.11. MODEX INDEMNIFICATION. Modex shall indemnify, defend and hold CTI and each of its officers, directors, employees, agents and consultants (each a "CTI Indemnitee") harmless from and against all third party costs, claims, suits, expenses (including reasonable attorneys' fees) and damages arising out of or resulting from (i) any breach or failure by Modex in the performance of its obligations under this Agreement, or (ii) the use by or administration to any Person of any Modex Licensed Products that arises out of sales of Modex Licensed Products by Modex, or a Modex Sublicensee (except where such cost, claim, suit, expense or damage arose or resulted from any negligence of CTI in the manufacture of any Modex Licensed Products by CTI, or the failure of CTI to manufacture Licensed Products in accordance with the specifications for such products), provided that the CTI Indemnitee gives reasonable notice to Modex of any such claim or action, tenders the defense of such claim or action to Modex and assists Modex at Modex's expense in defending such claim or action and does not compromise or settle such claim or action without Modex's prior written consent.

8.12. CTI INDEMNIFICATION. CTI shall indemnify, defend and hold Modex and each of its officers, directors, employees, agents and consultants (each a "Modex Indemnitee") harmless from and against all third party costs, claims, suits, expenses (including reasonable attorney's fees) and damages arising out of or resulting from (i) any breach or failure by CTI

in the performance of its obligations under this Agreement, or (ii) the use by or administration to any Person of any CTI Licensed Products that arises out of sales of CTI Licensed Products by CTI or a CTI Sublicense, or (iii) any negligence of CTI in the manufacture of Licensed Products by CTI, or the failure of CTI to manufacture Licensed Products in accordance with the specifications for such products, provided that such Modex Indemnitee gives reasonable notice to CTI of any such claims or action, tenders the defense of such claim or action to CTI and assists CTI at CTI's expense in defending such claim or action and does not compromise or settle such claim or action without CTI's prior written consent.

8.13. LIABILITY INSURANCE. Each Party shall maintain (subject to availability at a price common in the industry) (i) prior to the first commercial sale of a Licensed Product comprehensive general and products liability and completed operations insurance with a Best-rated A-XIV insurance company covering that Party's activities related to this Agreement in an amount of not less than $1,000,000 and (ii) during the remaining term of this Agreement either (1) net worth of no less than $50,000,000 or (2) comprehensive general and products liability and completed operations insurance covering that Party's activities related to this Agreement in an amount of not less than $5,000,000. Upon request, each Party shall provide to the other satisfactory evidence of that Party's compliance with this provision. The obligations under this Section 8.13 shall terminate upon the expiration of the statute of limitations applicable to any liability covered by the above-referenced insurance.

8.14. GOVERNING LAW. This Agreement shall be governed by and construed in accordance with the laws of the State of Rhode Island without regard to the conflict of laws provisions thereof.

8.15. NO DRAFTING PRESUMPTION. In construing the provisions of this Agreement, no presumption shall be made construing the provisions against either Party on the basis of such Party or such Party's counsel having drafted the provisions of this Agreement.

8.16. SUBMISSION TO JURISDICTION IN RHODE ISLAND. Modex hereby agrees to submit to the jurisdiction of the state and federal courts in the State of Rhode Island in regard to any dispute arising out of this Agreement which is not resolved as provided in Section 9.

9. RESOLUTION OF DISPUTES

9.1. GENERAL. In acknowledgment of the benefit to both Parties to resolve differences quickly and efficiently with as little disruption of each Parties' business as possible, the Parties agree to abide by the following provisions in connection with any dispute that should arise between the parties with respect to any matter relating to this Agreement, including any questions regarding the existence, validity or termination thereof.

9.2. DISPUTE RESOLUTION PROCESS.

(a) MEDIATION. In the event of any dispute between the Parties with respect to any matter relating to this Agreement, the Parties shall first use their best efforts to resolve such dispute among themselves. Prior to seeking any third party to resolve a dispute, the principal executive officers of CTI and Modex shall meet in a private meeting in New York, New York for at least one-half (1/2) of a day to attempt to resolve the dispute. If the Parties are unable to resolve the dispute within 30 days after the principal executive officers have met, the Parties will then seek the assistance of one or more unaffiliated third parties to assist in mediating the dispute.

(b) SELECTION OF ARBITRATORS. In the event that the Parties are unable to resolve a dispute within 30 days after commencement of mediation efforts, either Party may submit the matter to binding arbitration in accordance with the procedures set forth in this Section 9. If a Party intends to commence arbitration to resolve a dispute, such Party shall provide written notice to the other Party of such intention, and shall designate one arbitrator. Within 10 days of receipt of such notice, the other Party shall designate in writing a second arbitrator. The two arbitrators so designated shall, within 10 days thereafter, designate a third arbitrator. The arbitrators so designated shall not be employees, consultants, officers, directors or shareholders of or otherwise associated with either Party. Except as modified by the provisions of this Section 9, the arbitration shall be conducted in accordance with the rules of, and under the auspices of, the International Chamber of Commerce and the location of the arbitration shall be New York, New York. The language of such arbitration shall be English and all notices and written submissions provided in such proceeding shall be in English.

(c) WRITTEN PROPOSALS. Within 15 days after the designation of the third arbitrator, the arbitrators and the Parties shall meet at which time each Party shall be required to set forth in writing the issues which need to be resolved and a proposed ruling on each such issue. Written submissions shall be limited to 30 pages of text (not including exhibits which may include copies of agreements, or extracts from books and records, but not testimony affidavits).

(d) HEARING. The arbitrators shall set a date for a hearing, which shall be no later than 20 days after the submission of written proposals, to discuss each of the issues identified by the Parties. Each Party shall have the right to be represented by counsel. The arbitrators shall have sole discretion with regard to the admissibility of any evidence. Unless otherwise determined by unanimous agreement of the arbitrators the hearing shall be concluded in one day.

(e) RULING. The arbitrators shall use their best efforts to rule on each disputed issue within 20 days after the completion of the hearings described in subsection (d) above. The arbitrators shall, by majority decision, select the ruling proposed by one of the Parties as the arbitrators' ruling. The arbitrators' ruling shall be, in the absence of fraud or manifest error, binding and conclusive upon both Parties and may be enforced in a court of competent jurisdiction. The arbitrators may not award punitive or exemplary damages.

9.3. ARBITRATION COSTS. The arbitrators shall be paid a reasonable fee plus expenses, which fees and expenses shall be paid as designated by the arbitrators, or if the arbitrators do not so designate, such costs shall be shared equally by the Parties.

IN WITNESS WHEREOF, the Parties have caused this Agreement to be executed by their respective duly authorized officers as of the day and year set forth below, each copy of which shall for all purposes be deemed to be an original.

CYTOTHERAPEUTICS, INC.

By: /s/ IVOR ELRIFI

Ivor Elrifi, GENERAL COUNSEL, VICE PRESIDENT, SECRETARY
Date: October 29, 1997

MODEX THERAPEUTIQUES, SA

By: /s/ PATRICK AEBISCHER

Patrick Aebischer, PRESIDENT
Date: October 29, 1997

By: /s/ JACQUES ESSINGER

Jacques Essinger, DIRECTOR
Date: October 29, 1997

SCHEDULE 1.3.3

Confidential Information regarding the selection and development of cells and cell lines for encapsulated cell therapy, including such cells and cell lines themselves, including, without limitation, (i) Confidential Information regarding the development of so-called "hardy" cells (including, without limitation, cells engineered to [******* **** *** **]; cells engineered to [******* ******* ** *** ***** ********** ** * ******* ********]; and cells engineered for [* ********** **********]) and (ii) Confidential Information regarding the selection and development of human cells or cell lines derived from human cells for use in encapsulated cell therapy.

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* This confidential portion has been omitted and filed separately with the Commission

SCHEDULE 1.5

CTI PATENTS/PATENT APPLICATIONS--INCLUDED

The following patents and patent applications (including patents issued thereon), and any counterpart patents that issue claiming priority from these patents and patent applications, including, without limitation, additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions, renewals and foreign counterparts:

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* This confidential portion has been omitted and filed separately with the Commission

SCHEDULE 1.5A

CTI PATENTS/PATENT APPLICATIONS--NOT INCLUDED

The following patents and patent applications (including patents issued thereon), and any counterpart patents that issue claiming priority from these patents and patent applications, including, without limitation, additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions, renewals and foreign counterparts:

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* This confidential portion has been omitted and filed separately with the Commission

SCHEDULE 1.17.3

Confidential Information regarding the selection and development of cells and cell lines for encapsulated cell therapy, including such cells and cell lines themselves, including, without limitation, (i) Confidential Information regarding the development of so-called "hardy" cells (including, without limitation, cells engineered to [******* **** *** **]; cells engineered to [******* ******* ** *** ***** ********** ** * ******* ********]; and cells engineered for [* ********** **********]) and (ii) Confidential Information regarding the selection and development of human cells or cell lines derived from human cells for use in encapsulated cell therapy.

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* This confidential portion has been omitted and filed separately with the Commission

SCHEDULE 1.19

MODEX PATENTS/PATENT APPLICATIONS

The following patents and patent applications (including patents issued thereon), and any counterpart patents that issue claiming priority from these patents and patent applications, including, without limitation, additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions, renewals and foreign counterparts:

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* This confidential portion has been omitted and filed separately with the Commission

SCHEDULE 1.19A

MODEX PATENTS/PATENT APPLICATIONS--NOT INCLUDED

The following patents and patent applications (including patents issued thereon), and any counterpart patents that issue claiming priority from these patents and patent applications, including, without limitation, additions, divisions, continuations, continuations-in-part, substitutions, extensions, patent term extensions, renewals and foreign counterparts:

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* This confidential portion has been omitted and filed separately with the Commission

Exhibit 10.70

CYTOTHERAPEUTICS, INC.
701 George Washington Highway
Lincoln, RI 02865
(401) 288-1000

Dated as of September 30, 1997

Seth A. Rudnick, M.D.
CytoTherapeutics, Inc.
701 George Washington Highway
Lincoln, RI 02865

Re: Board Chairman and Consulting Positions

Dear Seth:

This letter will reflect our understanding in regard to your agreement to serve as Chairman of the Board of Directors of CytoTherapeutics, Inc. (the "Company") and as a Consultant to the Company.

1. Change in Position and Duties. Effective as of September 30, 1997, you will cease to serve as President and Chief Executive Officer of the Company. You will continue to serve as Chairman of the Board of Directors of the Company until the next Annual Meeting of the Stockholders of the Company and the provisions of this Agreement regarding your service as Chairman of the Board shall also apply during any further period in which you may be elected to such position. As Chairman of the Board, you will chair all meetings of the Board of Directors of the Company and will have those other duties and responsibilities, if any, specified for the Chairman of the Board of Directors of the Company in the By-laws of the Company, as the same may exist from time to time.

1.1. Transition Period. During the period commencing October 1, 1997 through December 31, 1997 (the "Transition Period"), you will make yourself available as requested by the Company's Chief Executive Officer to fulfill such other duties and responsibilities as the Chief Executive Officer may reasonably expect, consistent with your status as

the current Chairman of the Board of Directors of the Company and former President and Chief Executive Officer of the Company and with any applicable provisions of this Agreement. In this regard it is expected that you will devote approximately one day per week to in-office consultation with the Chief Executive Officer and other members of the Company's senior management; that you will travel on Company business as the Chief Executive Officer may reasonably request for an additional one or two days per week; and that you will make yourself generally available as required at other times during normal business hours to consult by telephone regarding the business of the Company.

1.2. Consulting Period. From January 1, 1998 through December 31, 1999 (the "Consulting Period"), you will serve as a Consultant to the Company and shall provide such consulting services to the Company as the Company's Chief Executive Officer may reasonably request from time to time up to a maximum commitment of 5 days per month and 50 days per year of such consulting services.

2. Salary and Bonus.

2.1. Transition Period. During the Transition Period, your salary shall be paid at an annual rate of $200,000 per year.

2.2. 1997 Bonuses. The Board of Directors will review your performance in all positions you have held with the Company during 1997 and you shall be eligible to receive a bonus at least equal to the bonus you would have been eligible to receive under your employment contract as President and CEO for the time during 1997 in which you served in such capacity (up to (9 months/12 months) x 20% x $300,000 = $45,000).

2.3. Consulting Period Payments. For your services as a Consultant and, to the extent applicable, Chairman and a member of the Board of Directors of the Company, during the Consulting Period you shall be paid a consulting fee of $12,500 per month, plus reimbursement for any out-of-pocket expenses reasonably incurred by you in the course of performing such services, subject to appropriate documentation of such expenses on a basis consistent with Company policy. During the Consulting Period you shall not receive any other compensation for any service you may render as a member of the Board of Directors of the Company or as Chairman thereof; should you serve in any such position after the end of the Consulting Period, you shall be compensated therefore according to the Company's then-existing policies for the compensation of a non-employee holding any such position.

2.4. Vacation Pay. No later than January 15, 1998, you shall be paid $25,000 as a lump sum payment in lieu of all unused vacation time accrued by you during your service as Chief Executive Officer of the Company.

3. Stock Options. During the Transition Period and the Consulting Period, stock options granted to you and not yet expired, exercised, canceled or otherwise become unexerciseable shall continue to vest. In addition, subject to approval by the Company's Board of Directors, the exercise period for all options previously granted to you shall be extended until the end of the Consulting Period (i.e., all options may be exercised at any time prior to December 31, 1999 and must be exercised no later than that date).

4. Benefits.

4.1. Health and Dental. During the Transition Period and the Consulting Period, to the extent permitted by the terms of the Company's group health and dental plan and by its health and dental plan insurer or providers, as applicable, the Company will continue your participation and that of your eligible dependents in its group health and dental plan to the same extent as you and they currently participate and will pay the premium cost of such participation, to the same extent currently paid, through the earlier of (i) the end of the Consulting Period or (ii) the date you commence other employment which makes you eligible, at no greater cost to you than the current cost to you, if any, under the Company's health and dental plans, to obtain comparable coverage under the health and dental plans of your new employer. If the Company is unable to provide continuation as contemplated in the previous sentence, you may exercise your right to continue your coverage and that of your eligible dependents in the Company's group health and dental plan under the federal law known as COBRA, provided you are eligible to do so, and, if you are eligible, then, until the end of the Consulting Period or the date you cease to be eligible for continuation under COBRA, the Company will pay the premium cost of your coverage and that of your eligible dependents.

4.2. Life Insurance. During the Transition Period and the Consulting Period, to the extent permitted by the terms of the Company's group life insurance plan, the Company will continue your coverage under its group life insurance plan in the same face amount in which your life is currently insured under such plan through the end of the earlier of (i) the Consulting Period or (ii) the date you commence other employment

under circumstances which entitle you to group life insurance coverage comparable to that provided by Company at no greater cost to you than such coverage as currently provided to you by the Company. If life insurance coverage is not available under the Company's plan, the Company shall pay $2,500 per year toward the cost of any life insurance coverage which you may arrange.

4.3. Plan Limitations. It is understood and agreed that the benefits of the group health and group life insurance plans of the Company are subject to such conditions and limitations as are set forth in the applicable plan, policy or contract terms, as such may exist from time to time, and that any disputes concerning eligibility for payment of benefits under such plan shall be settled in accordance with the terms thereof, and that the Company shall have no liability to you, your dependents or any other person claiming through you, for payment of benefits under any such plan.

4.4. Retirement Annuity. Commencing at the time you reach age 60 and continuing until your death, the Company shall pay to you a monthly retirement payment at the rate of $30,000 per year. You acknowledge that this payment obligation is an unsecured payment obligation of the Company that has not been (and is not expected to be) funded by the Company through the purchase of an annuity contract or otherwise.

4.5. Office Space. During the time you serve as Chairman of the Board of the Company, the Company shall make available to you office space, either at the Company, or at the Company's option, at a separate location located no more than one-half hour from the Company, for you to use. If the Company elects to provide you with a separate office location, the cost to the Company (including rent, secretarial services, leased equipment, etc.) shall not exceed $2,000 per month.

5. During the Transition and Consulting Periods and for one year thereafter, you will not, either directly or indirectly, become employed by, serve as a director of or consultant to or otherwise participate in any competitor of the Company. A competitor shall be defined as any entity utilizing or proposing to utilize the transplantation of cells as a therapeutic agent for the treatment of human disease. You further agree that during the Transition and Consulting Periods and for a period of one year thereafter, you will not directly or indirectly solicit the services of any employee of the Company for another entity, or otherwise induce or attempt to induce any such employee to leave the employ of the Company.

6. You shall not disclose to any other person, corporation or other entity (except as required by applicable law or for the proper performance of your duties and responsibilities hereunder), or use for your own benefit or gain, any Confidential Information of the Company. Confidential Information of the Company shall mean all information of or regarding the Company other than information that is generally known to the public through no fault of yours, including, without limitation, information regarding the research and development activities of the Company, the products and services of the Company, the cost, sources of supply and strategic plans of the Company, the identity and special needs of the customers of the Company and those persons and organizations with whom the Company has business relationships and the nature of those relationships, as well as any comparable information that the Company may possess regarding customers or others who do business with the Company.

If the terms of this Letter Agreement accurately reflect your understanding of the matters set forth herein, please sign this Agreement and return it to the Company. The enclosed copy of this Letter Agreement, which you should also sign and date, is for your records.

Sincerely,

CYTOTHERAPEUTICS, INC.

By:_____
Name:
Title:

Accepted and Agreed:

/s/ Seth Rudnick
- --------------------------
Seth A. Rudnick, M.D.

Exhibit 10.74

CYTOTHERAPEUTICS, INC.
Two Richmond Square
Providence, RI 02906
401-272-3310

September 25, 1997

Richard M. Rose, M.D.
6826 LaValle
Plateada
P.O. Box 567
Rancho Santa Fe, CA 92067

Dear Richard:

This letter will confirm our offer to you of employment with CytoTherapeutics, Inc. (the "Company") under the terms and conditions that follow:

1. Position and Duties. As of the Effective Date, as such term is defined in the Agreement and Plan of Merger among the Company, CTI Acquisition, Inc., StemCells, Inc., you and certain other individuals dated August 13, 1997, you will be employed by the Company hereunder on a full-time basis as its President and Chief Executive Officer. In addition, and without further compensation, you agree to service as a member of the Board of Directors of the Company (the "Board") and as a director or officer of one or more of the Company's Affiliates, as defined below, if so elected or appointed from time to time. As President and Chief Executive Officer, you will be expected to exert your full-time best efforts to promote and protect the business interests of the Company. Specifically, but not exclusively, your responsibilities will be to manage the operations of the Company, to build and maintain an outstanding and harmonious working team of both scientific and professional employees, to secure, promote and maintain the appropriate financing and capital structure of the Company, to manage and direct the strategic development of the Company's business plan and its implementation and to oversee the overall scientific affairs of the Company. You will report directly to the Board.

2. Salary and Bonus. For all services that you perform for the Company and its Affiliates, the Company will provide you compensation during your employment in accordance with this Paragraph 2. Your base salary will be at the rate of Two Hundred and Seventy-Five Thousand Dollars ($275,000) per year. Your performance and compensation will be reviewed at least annually by the Compensation Committee of the Board. In

addition to your base salary, you will eligible, at the end of calendar year, beginning with calendar 1998, during your employment hereunder, for a bonus of up to twenty-five percent (25%) of your base salary, the amount of each such bonus being determined by the Board in its discretion.

3. Stock Options.

a. Through the CytoTherapeutics, Inc. 1992 Equity Incentive Plan (the "Incentive Plan"), and subject to the terms and conditions of such Plan, you will be granted an option to acquire 200,000 shares of the common stock of the Company (the "Time-Based Option") at the fair market value of such shares on the Effective Date, as determined by the Board. Subject to your continued employment by the Company, the Time-Based Option will vest over forty-eight (48) months as follows: (i) one quarter of the shares will vest on the first anniversary of the Effective Date and (ii) the remaining shares shall vest at the rate of one forty-eighth (1/48) per month on the last day of each month during the ensuing thirty-six months. Except as otherwise expressly provided herein, the Time-Based Option shall be governed by the terms of the Incentive Plan, as in effect from time to time. Any Change in Control will result in the accelerated vesting of the option to acquire 100% of such shares. A Change in Control shall mean any consolidation or merger in which the Company is not the surviving corporation, a transaction or series of related transactions that result in the acquisition of all of substantially all of the Company's outstanding Common Stock by a single person or entity or by a group of persons or entities acting in concert, or the sale or transfer of all or substantially all of the Company's assets.

b. In addition to the Time-Vested Option, the Company will grant you an option to acquire 100,000 shares of the common stock of the Company (the "Performance-Based Option") at fair market value of such shares on the Effective Date, as determined by the Board. The Performance-Based Options are subject to the terms of the Performance-Based Incentive Option Agreement, a copy of which is attached hereto as Schedule A, and to your execution of that Option Agreement.

c. In addition to the foregoing options, you shall be eligible, at the end of any calendar year beginning with calendar year 1998, or as otherwise determined from time to time by the Board or the Compensation Committee of the Board, to receive additional options, the amount and terms of any such options to be determined by the Board or such Compensation Committee in their sole discretion.

4. Relocation and Relocation Allowance. Promptly following the Effective Date, you will establish your principal office at the Company's offices in Rhode Island and a temporary residence for yourself within driving distance of such office. You will relocate permanently to the Rhode Island area no later than July 31, 1998. The allocation of your time between the Company's operations in Rhode Island, the Company's operations in

California and travel elsewhere on Company business will, in your role as President and CEO of the Company, be primarily determined by you; however, you will not spend an average of more than one business day per week during any calendar quarter in California without approval of the Board. The Company will provide you with One Hundred and Twenty Five Thousand Dollars ($125,000) for relocation, temporary housing and related expenses, which sum shall be payable to you $75,000 on execution and delivery of this Agreement and $50,000 upon your permanent relocation to Rhode Island as provided above. In addition, the Company will provide you with an interest-free bridge loan in an amount (not to exceed $200,000) reasonably required by you in order to purchase a house within driving distance of the Company's offices in Rhode Island, such loan to be secured by a second mortgage on such house and to be payable by you at the time of the sale of your residence in California. You agree to use reasonable efforts to sell such residence.

5. Benefits. You will be entitled to participate in any and all employee benefit plans from time to time in effect for senior management of the Company generally, except to the extent that such plans are duplicative of benefits otherwise provided to you under this Agreement. Such participation shall be subject to (i) the terms of the applicable plan documents, (ii) generally applicable policies of the Company and (iii) the discretion of the Board and plan administrators, as provided for in or contemplated by such plan. The Company will provide you with a leased automobile, the cost of which will be paid by you and the Company in proportion to your business and personal use of such automobile. Prior to your permanent relocation to within driving distance of the Company's principal offices, the Company will reimburse you for the cost of two round trips per month to southern California. The Company expects that these trips will generally be made in connection with Company business and that you will attempt, to the extent possible, to schedule any personal trips to coincide with such business. The Company will provide you with four weeks vacation per year. The Company shall reimburse you for all expenses reasonably incurred by you in connection with your performance of your duties hereunder on a basis consistent with Company policies.

6. Confidentiality and Restricted Activities. You agree that some restrictions on your activities during and after employment are necessary to protect the goodwill, Confidential Information and other legitimate interests of the Company:

a. During your employment and thereafter, except as required by applicable law or for the proper performance of your duties and responsibilities to the Company, you shall not use or disclose to any Person any Confidential Information, as defined below. This restriction shall continue to apply after your employment terminates, regardless of the reason for such termination.

b. While you are employed by the Company and for a period of one (1) year thereafter, you will not, directly or indirectly, engage in any activity, whether as

owner, partner, investor, consultant, employee, agent or otherwise, that is competitive with the business of the Company or its Affiliates, provided, however, that nothing contained in this paragraph shall prohibit you from owning up no more than one percent (1%) of the outstanding stock of any publicly traded company.

c. While you are employed by the Company and for a period of one (1) year thereafter, you will not, directly or indirectly, hire or attempt to hire any employee of the Company or its Affiliates, assist in such hiring by any Person or otherwise solicit, induce or encourage any employee of the Company or any of its Affiliates to terminate his or her relationship with them.

d. You agree that you will not, during your employment with the Company, improperly use or disclose any proprietary information or trade secrets of any former or concurrent employer or other Person with whom you have an agreement or duty to keep in confidence information acquired by you in confidence, if any. You also agree that you will not bring onto Company premises any unpublished document or proprietary information belonging to any such employer or other Person, unless consented to in writing by such employer or other Person.

e. All documents, records, tapes, software and other media of every kind and description relating to the business, present or otherwise, of the Company and its Affiliates and any copies, in whole or in part, thereof (the "Documents"), whether or not prepared by you, shall be the sole and exclusive property of the Company and its Affiliates. You agree to safeguard all Documents and to surrender to the Company at the time your employment terminates, or at such earlier time or times as the Board may specify, all Documents and other property of the Company and its Affiliates (including without limitation, devices and equipment) then in your possession or control.

f. You agree that the Company shall, in addition to any other remedies available to it, be entitled to preliminary and permanent injunctive relief against any breach by you of the covenants contained in this Paragraph 6, without having to post bond. In the event that any provision of this Paragraph 6 shall be determined by a court of competent jurisdiction to be unenforceable by reason of its being extended over too great a time, too large a geographic area or too great a range of activities, it shall be interpreted to extend only over the maximum period of time, geographic area or range of activities as to which it may be enforceable.

g. For purposes of this Agreement:

i. A business shall be deemed to be competitive with the Company or its Affiliates if it engages or proposes to engage in any business activity which is both (A) utilizing or seeking to develop technology capable of utilizing the transplantation

of cells as a therapeutic agent for the diagnosis, prevention or treatment of human disease, injury or condition and (B) in any field the Company or any of its Affiliates is then pursuing or then has in contemplation or planning.

ii. "Affiliates" means all persons and entities directly or indirectly controlling, controlled by or under common control with the Company, where control may be by management authority, equity interest or otherwise.

iii. "Confidential Information" means any and all information of the Company and its Affiliates that is not generally known by others with whom they compete or do business or with whom they plan to compete or do business and any and all information, publicly known in whole or in part or not, which, if disclosed by the Company or its Affiliates, would assist in competition against them. Confidential Information includes without limitation such information relating to (i) the development, research, testing, production and marketing activities of the Company and its Affiliates, (ii) the products and services of the Company and its Affiliates, (iii) their patents, trade secrets, licenses and intellectual property, patients and clinical trials; (iv) the costs, sources of supply, financial performance and strategic plans of the Company and its Affiliates, (v) the identity and special needs of the customers of the Company and its Affiliates and (vi) the people and organizations with whom the Company and its Affiliates have business relationships and those relationships. Confidential Information also includes information that the Company or any of its Affiliates has received belonging to others with any understanding, express or implied, that it would not be disclosed. Confidential Information does not include, however, information that has become publicly known and generally available other than through a wrongful act by you or any other Person owing a duty of confidentiality to the Company or any of its Affiliates.

iv. "Person" means an individual, a corporation, an association, a partnership, an estate, a trust and any other entity or organization, other than the Company or any of its Affiliates.

7. Inventions.

a. You hereby represent to the Company and agree that, except as described in Schedule B hereof, you have no inventions, original works of authorship, developments, improvements or trade secrets that were made by you prior to your employment with the Company and which relates to the Company's current or proposed business, products or research and development.

b. You will promptly make full written disclosure to the Company, hold in trust for the Company's sole right and benefit and hereby assign and agree to assign to the Company or its designee all of your right, title and interest in any and all Inventions.

As used in this Agreement, "Inventions" means inventions, discoveries, developments, methods, processes, compositions, works, concepts and ideas (whether or not patentable or copyrightable or constituting trade secrets) conceived, made, created, developed or reduced to practice by you (whether alone or with others and whether or not during normal business hours or on or off Company premises) during your employment that relate in any way to the business, products or services of the Company or any of its Affiliates or to any prospective activity of the Company or any of its Affiliates or for which the Confidential Information or the Company's facilities have been utilized. You further acknowledge and agree that all original works of authorship made by you solely or jointly with others within the scope of your employment and eligible for protection by copyright are "works made for hire," as that term is defined in the United States Copyright Act. You agree to keep and maintain adequate and current records of all Inventions made by you solely or jointly with others during your employment with the Company. Such records will be in the form of notes, sketches, drawings or any other format that may be specified by the Company These records will be available to, and remain the sole property of, the Company at all times. You agree to assist the Company or its designee, at the Company's expense, in every proper way, to secure the Company's rights in the Inventions and copyrights, including without limitation disclosure to the Company of all pertinent information and data with respect thereto, the execution of all applications, specifications, oaths, assignments and all other instruments that the Company shall deem necessary or desirable in order to apply for and obtain such rights, and in order to assign and convey to the Company, its successors, designees and nominees the sole and exclusive right, title and interest in and to such Inventions, and any copyrights, patents, or other intellectual property rights relating thereto, both during your employment by the Company and thereafter. In the event that the Company is unable for any reason to secure or to prosecute any patent application with respect to any of such Inventions (including without limitation, renewals, extensions, continuations, divisions or continuations in part thereof), you hereby irrevocably designate and appoint the Company and its duly authorized officers and agents as your agents and attorney-in-fact to act for and in your behalf and instead of you, to execute and file any such application and to do all other lawfully permitted acts to further the prosecution and issuance of patents thereof with the same legal force and effect as if executed by you. You agree that you will assist the Company in the prosecution and enforcement of the Company's rights to the Inventions and copyrightable materials after termination of your employment, at the Company's expense.

8. Termination and Termination Benefits. Your employment with the Company is "at will," which means that either you or the Company may terminate your employment at any time, with or without cause or good reason.

a. The Company may terminate your employment other than for "cause" at any time upon written notice to you and, in that event, (i) the Company will continue to pay you your base salary for the longer of (A) one year following the date of such

termination or (B) two years following the date of such termination in the case of any such termination occurring in connection with a Change in Control or (C) until the third anniversary of the Effective Date, provided, however, that the Company's obligation, if any, to pay such base salary on and after the second anniversary of such termination shall be reduced, on a dollar-for-dollar basis, by your total pre-tax compensation from any employment (including self-employment). If subjection (C) applies, you agree to seek such employment and accurately and promptly to report to the Company any such compensation derived therefrom. In addition, the Time-Based Option will become fully vested as to all unvested shares covered by such option as of the date your employment terminates. To the maximum extent permitted by the Company's benefit plans, all benefits provided to you hereunder shall continue for the longer of (A) one year following the date of such termination or (B) two years following the date of any such termination which occurs in connection with a Change in Control. The Company shall not be obligated to purchase any special insurance or other coverage in order to satisfy the foregoing obligation.

b. The Company may terminate your employment upon written notice to you in the event that you become disabled during your employment through any illness, injury, accident or condition of either physical or psychological nature and, as a result, you are unable to perform substantially all of your duties and responsibilities hereunder for ninety (90) days during any three hundred and sixty-five (365) calendar days. In that event, the Company will continue to pay you your base salary (i) for a period of six (6) months following such termination or (ii) until you obtain other employment or (iii) until you become eligible for disability income under any disability income plan provided by the Company, whichever of these events shall first occur.

c. The Company may terminate your employment hereunder for cause at any time upon written notice to you setting forth in reasonable detail the nature of such cause. The following, as determined by the Company in its reasonable judgment, shall constitute "cause" for termination: (i) your willful failure to perform your material duties and responsibilities to the Company and its Affiliates (including, without limitation, those duties and responsibilities described in Section 1) and; (ii) your material breach of Paragraph 6 or Paragraph 7 of this Agreement; (iii) fraud, embezzlement or other material dishonesty with respect to the Company or any of its Affiliates; or (iv) your conviction of, or plea of nolo contendere to, a felony.

d. You may terminate your employment at any time, with or without good reason, upon written notice to the Company. If you decide to terminate your employment without good reason, you agree to give the Company three months' notice of termination. You may terminate your employment hereunder with good reason at any time upon written notice to the Company. The following shall constitute "good reason" for termination: material breach by the Company of any provision of this Agreement, including, without limitation, any material diminution in your authority or responsibilities from that

contemplated by Section 1 hereof, which breach continues for more than ten (10) business days following receipt by the Company of written notice from you setting forth in reasonable detail the nature of such breach. If you terminate your employment with good reason, the Company will be obligated to you under Paragraph 8.a hereof as if the Company had terminated your employment other than for cause.

e. If you resign without good reason or your employment is terminated by the Company for cause, the Company shall have no further obligation to you other than for base salary earned through the date of termination. No severance pay or other benefits of any kind will be provided.

9. Withholding. All payments and reimbursements made by the Company under this Agreement shall be reduced by any tax or other amounts required to be withheld by the Company under applicable law.

10. Assignment. Neither you nor the Company may make any assignment of this Agreement or any interest herein, by operation of law or otherwise, without the prior written consent of the other; provided, however, that the Company may assign its rights and obligations under this Agreement without your consent to one of its Affiliates or to any Person with whom the Company shall hereafter affect a reorganization, consolidation or merger or to whom the Company transfers all or substantially all of its properties or assets. This Agreement shall inure to the benefit of and be binding upon you and the Company and each of your respective successors, executors, administrators, heirs and permitted assigns.

11. Waiver. Except as otherwise expressly provided in this Agreement, no waiver of any provision hereof shall be effective unless made in writing and signed by the waiving party. The failure of either party to require performance of any term or obligation of this Agreement, or the waiver by either party of any breach of this Agreement, shall not prevent any subsequent enforcement of such term or obligation or be deemed a waiver of any subsequent breach.

12. Severability. If any portion or provision of this Agreement shall to any extent be declared illegal or unenforceable by a court of competent jurisdiction, then the remainder of this Agreement, or the application of such portion or provision in circumstances other than those as to which it is so declared illegal or unenforceable, shall not be affected thereby, and each portion and provision of this Agreement shall be valid and enforceable to the fullest extent permitted by law.

13. Notices. Except as otherwise expressly provided herein, any notices, requests, demands and other communications provided for by this Agreement shall be in writing and shall be effective when delivered in person or deposited in the United States mail, postage prepaid, registered or certified, and addressed to you at your last known

address on the books of the Company or, in the case of the Company, at its main office, attention of the Chairman of the Board.

14. Captions. The captions and headings in this Agreement are for convenience only and in no way define or describe the scope or content of any provision of this Agreement.

15. Entire Agreement. This Agreement sets forth the entire agreement and understanding between you and the Company and supersedes all prior communications, agreements and understandings, written and oral, with respect to the terms and conditions of your employment. This Agreement may not be amended or modified, except by an agreement in writing signed by you and the Chairman of the Board or other specifically authorized representative of the Company.

16. Governing Law. This Agreement shall be governed, construed and enforced in accordance with the laws of Rhode Island, without regard to the conflict of laws principles thereof.

17. No Conflicting Agreements. You hereby represent to the Company that neither your execution and delivery of this Agreement nor your acceptance of employment with the Company nor your performance under this Agreement will conflict with or result in a breach of any of the terms, conditions or provisions of any agreement to which you are a party or are bound or any order, injunction, judgment or decrees of any court or governmental authority or any arbitration award applicable to you.

18. Compliance with Agreement. The Company's obligations under this Agreement and its obligation to deliver stock under the terms of the stock options granted pursuant to the terms of this Agreement (or otherwise granted you during the course of your employment) are conditioned on your compliance with the terms and conditions of this Agreement and the accuracy of the representations made to the Company by you herein.

19. Agreement Void. If the Effective Date does not occur, for any reason whatsoever, this agreement shall be null and void and of no force or effect.

If the foregoing is acceptable to you, please sign the enclosed copy of this letter in the space provided below and return it to me, whereupon this letter and such copy will constitute a binding agreement between you and the Company on the basis set forth above as of the date first above written.

Sincerely yours,
CYTOTHERAPEUTICS, INC.

By: /s/ Seth A. Rudnick

Seth A. Rudnick, M.D.
Chairman

Accepted and agreed:

/s/ Richard M. Rose
- ---
Richard M. Rose, M.D.

Date: _____

Schedule A

Performance-Based Incentive Option Agreement

Optionee: Richard M. Rose Shares Subject to Option: 100,000
Dated: September 25, 1997

CYTOTHERAPEUTICS, INC.

PERFORMANCE-BASED INCENTIVE OPTION AGREEMENT

This Agreement is made as of the date set forth above by and between CytoTherapeutics, Inc., a Delaware corporation (the "Company" or "CTI"), and the Optionee specified above (the "Optionee").

WHEREAS, Optionee has entered into a Consulting or Employment Agreement with the Company which provides for the grant of the options evidenced hereby (the "Consulting/Employment Agreement"); and

WHEREAS, Optionee is in a position to make a significant contribution to the long-term success of the Company, and in particular the Company's stemcell research program.

NOW, THEREFORE, the Company and Optionee agree as follows:

1. Grant of Option. This agreement evidences the grant by the Company to Optionee pursuant to the Company's 1997 Stemcells Research Stock Option Plan (the "Plan") of an option to purchase, in whole or in part, on the terms provided herein, the number of shares specified above of the Company's Common Stock, $.01 par value (the "Common Stock"), at a per share price equal to $5.25 (the "Option"). This Option is not intended to qualify as an "incentive stock option" within the meaning of Section 422 of the Internal Revenue Code of 1986, as amended. This Option shall terminate on the tenth anniversary of the date of this Agreement (the "Final Exercise Date"), and is subject to earlier termination as provided in Sections 6 and 7 below.

2. Exercisability of Option. Subject to the terms and conditions hereof, this Option shall vest and become exercisable as follows:

Milestone	% of Shares Vesting
On the date of this Agreement	6.25%
First Corporate Partnership (as defined below) (before September 1, 1998)	

If > $5,000,000 and $10,000,000	6.25%
If > $10,000,000 and $15,000,000	8.75%
If > $15,000,000	11.25%
Second Corporate Partnership (before September 1, 1999)	
If > $5,000,000 and $10,000,000	6.25%
If > $10,000,000 and $15,000,000	8.75%
If > $15,000,000	11.25%
First Corporate Partnership resulting from discovery of a new stem cell (before June 30, 2000)	
If > $5,000,000 and $10,000,000	6.25%
If > $10,000,000 and $15,000,000	8.75%
If > $15,000,000	11.25%
Second Corporate Partnership resulting from discovery of a new stem cell (before June 30, 2000)	
If > $5,000,000 and $10,000,000	6.25%
If > $10,000,000 and $15,000,000	8.75%
If > $15,000,000	11.25%
Commencement of first clinical trial of a CTI stem cell product (before June 30, 2000)	12.50%
Filing of first United States regulatory filing for marketing approval of a CTI stem cell product (before June 30, 2003)	12.50%
Filing of first European Union or Japanese regulatory filing for market	12.50%

approval with respect to a CTI stem cell product (before June 30, 2004)	
First United States commercial approval of a CTI stem cell product (before June 30, 2005)	25.00%
First European Union or Japanese commercial approval of a CTI stem cell product (before June 30, 2005)	25.00%

For purposes of the foregoing, "Corporate Partnership" means any joint venture, licensing agreement, collaboration agreement, or research and development agreement to which the Company is a party and which is material to the long-term success of the Company. A "Corporate Partnership resulting from the discovery of a new stem cell" shall mean a Corporate Partnership which is formed to commercially develop technology resulting from research conducted pursuant to the Research Plan (as such term is defined in a letter agreement between the Company and Messrs. Weissman, Gage and Anderson, dated as of September __, 1997) which the corporate partner and CTI reasonably believe has resulted in the discovery of a previously undiscovered stem cell. The dollar amounts set forth above with respect to Corporate Partnerships refer to the receipt by the Company of the aggregate amount of the following payments received in connection with any such Corporate Partnership:

(i) any non-refundable up-front license fees;

(ii) the present value of all non-refundable, non-contingent license fees payable at a later date;

(iii) the amount by which the purchase price paid for any non-refundable, non-contingent equity investment in the Company made in connection with such Corporate Partnership exceeds the fair market value of such equity investment as reasonably determined by the Board of Directors of the Company; and

(iv) 50% of all non-contingent payments for sponsored research under any sponsored research agreement, provided, however, that in the case of the $5 million target in each of the first two corporate partnership milestones, 100% of such payments shall count toward satisfaction of such target.

The Company shall not structure any Corporate Partnership in a bad faith effort to avoid giving rise to the vesting of options hereunder.

3. Exercise of Option. Each election to exercise this Option shall be in writing, signed by Optionee or by his duly appointed guardian or representative, his executor or administrator or the person or persons to whom this Option is transferred by will or the applicable laws of descent and distribution (collectively, the "Legal Representative"), and received by the Company at its principal office in Providence, Rhode Island, accompanied by payment in full as provided in Section 4 below. In the event this Option is exercised by such Legal Representative, the Company shall be under no obligation to deliver stock hereunder unless and until the Company is reasonably satisfied that the person or persons exercising this Option is or are the duly appointed guardian(s) or representative(s) of Optionee, the duly appointed executor(s) or administrator(s) of the deceased Optionee or the person or persons to whom this Option has been transferred by will or the applicable laws of descent and distribution.

4. Payment for Stock. Shares of Common Stock shall be issued only upon receipt by the Company of full payment of the purchase price for the shares as to which this Option is exercised. The purchase price is payable by Optionee to the Company either (i) in cash or by certified check or cashier's check payable to the order of the Company; or (ii) through the delivery of shares of Common Stock (duly owned by Optionee and as to which Optionee has good title free and clear of any liens and encumbrances) which have been outstanding for at least six months and which have a fair market value (as determined by the Board of Directors of the Company) on the last business day prior to the date of exercise of this Option equal to the purchase price; or (iii) by delivery of an unconditional and irrevocable undertaking by a broker to deliver promptly to the Company sufficient funds to pay the exercise price; or (iv) by any combination of the forgoing permissible forms of payment. The Company will not be obligated to deliver any shares unless and until, in the opinion of the Company's counsel, all applicable federal and state laws and regulations have been complied with, nor, in the event the outstanding Common Stock is at the time listed upon any stock exchange, unless and until the shares to be delivered have been listed or authorized to be listed upon official notice that legal matters in connection with the issuance and delivery of such shares have been approved by the Company's counsel. The Company will use its best efforts to effect any such compliance or listing, and Optionee agrees to take any action reasonably requested by the Company in connection therewith. Subject to any applicable limitations under the Securities Act of 1933, as amended, and the rules and regulations thereunder, the Company will promptly file a Registration Statement on Form S-8 (or any successor form), with respect to the shares of Common Stock issuable upon exercise of this Option, and the Company will use all reasonable efforts to maintain the effectiveness of such registration statement for so long as this Option shall remain outstanding. The Company may require that Optionee agree that he will notify the Company when he makes any disposition of the shares issued upon exercise of this Option whether by sale, gift or otherwise. Optionee will have the rights of a shareholder only as to shares actually acquired by him upon exercise of this Option.

5. Non-transferability of Option. This Option may not be transferred by Optionee otherwise than by will or by the laws of descent and distribution. During Optionee's lifetime this Option may be exercised only by Optionee or Optionee's duly appointed guardian or representative.

6. Termination of Service. In the event Optionee ceases to be a consultant to or employee of the Company because the Company terminates his service for Cause (as defined in the Consulting/Employment Agreement) or Optionee terminates his service without Good Reason (as defined in the Consulting/Employment Agreement), this Option shall immediately terminate except that Optionee may thereafter exercise this Option, to the extent he was entitled to exercise it on the date when his service terminated, for a period of 90 days after the date of such termination. In no event, however, may this Option be exercised after the Final Exercise Date.

7. Death or Disability. In the event Optionee dies or Optionee's service with the Company terminates by reason of disability (meaning the inability of Optionee, because of physical or mental illness or injury, to perform substantially all of his duties and responsibilities to the Company), this Option shall continue to be eligible for vesting as set forth in Section 2 of this Agreement for a period of two years after Optionee's death or the termination of his service because of disability. In addition, this Option may be exercised, as to all or any of (a) the shares that Optionee was entitled to purchase immediately prior to his death or the termination of his service because of disability and (b) the shares that vest in accordance with the preceding sentence, by Optionee or his Legal Representative, at any time or times within three years after his death or such termination of service. Except as so exercised this Option will expire at the end of such period. In no event, however, may this Option be exercised after the Final Exercise Date.

8. Administration. This Option will be administered by the Board of Directors of the Company, which will have the authority to interpret this agreement and to decide all questions and settle all controversies and disputes which may arise in connection herewith. All decisions, determinations and interpretations of the Board of Directors will be binding on all parties concerned. A majority of the members of the Board of Directors will constitute a quorum, and all determinations of the Board of Directors will be made by a majority of its members. Any determination of the Board of Directors under this agreement may be made without notice or meeting of the Board of Directors by a written instrument signed by a majority of the members of the Board of Directors. In the event of any conflict between the terms of this Option and the terms of the Plan the terms of this Option will control.

9. Stock to be Delivered. Stock to be delivered upon exercise of this Option may constitute an original issue of authorized but unissued stock or may consist of previously issued stock acquired by the Company as determined from time to time by the

Board of Directors. The Board of Directors and the proper officers of the Company will take any appropriate action required for such delivery.

10. Changes in Stock. In the event of a stock dividend, stock split or combination of shares, recapitalization or other change in the Company's capital structure, the Board of Directors of the Company (whose determination will be binding on Optionee) will make appropriate adjustments to the number and kind of shares of stock or other securities subject to this Option, the exercise price and other relevant provisions. Except as provided in the following paragraph, in the event of a Change in Control (as defined below), this Option will expire and cease to be exercisable, provided that at least twenty days prior to the effective date of any such Change in Control, the Board of Directors shall either (a) make this Option immediately exercisable in full, or (b) arrange to have the acquiror or an affiliate thereof grant a replacement option or other replacement award containing terms that the Board of Directors reasonably determines to be equitable under the circumstances. "Change in Control" means any consolidation or merger in which the Company is not the surviving corporation, a transaction or series of related transactions that result in the acquisition of all or substantially all of the Company's outstanding Common Stock by a single person or entity or by a group of persons or entities acting in concert, or the sale or transfer of all or substantially all of the Company's assets.

11. Acceleration of Options on Change in Control. Any Change in Control will result in the accelerated vesting of the lesser of (i) 50% of the shares originally issuable pursuant to this Option or (ii) all of the shares which would become vested on the achievement of all milestones which are not time-barred at the time of Change in Control.

In addition, the Shares subject to this Option shall be accelerated under the circumstances and to the extent described in Section 1 (f) of the Agreement (the "Research Agreement") dated September 25, 1997 among the Company, Irving Weissman and Fred H. Gage.

12. Amendments. The Board of Directors of the Company may at any time or times amend this Option for the purpose of satisfying the requirements of any changes in applicable laws or regulations or for any other purpose which may at the time be permitted by law, provided that no such amendment will adversely affect the rights of Optionee without his consent.

13. Governing Law. This agreement shall be governed by and construed in accordance with the laws of the State of Delaware (not including the conflict of laws principles thereof).

IN WITNESS WHEREOF, the Company has caused this agreement to be executed by its duly authorized officer. This Option is granted at the Company's office, on the date stated above.

CYTOTHERAPEUTICS, INC.

By:_____
President

Accepted and Agreed:

_____
Optionee

Schedule B

Prior Inventions

None.

Exhibit 10.75

Two Richmond Square
Providence, RI 02906
401.272.3310
FAX 401.272.3485

CytoTherapeutics

April 17, 1997

John S. McBride
5 Olde Connecticut Path
Westborough, MA 01581

Dear John:

This letter will confirm our understanding regarding your employment by CytoTherapeutics, Inc. (the "Company") as Senior Vice President, Business Operations and Chief Financial Officer.

1. Joining the Company. You will begin your employment with the Company on the Starting Date, which will be June 2,1997, unless we mutually agree on a different Starting Date.

2. Position and Duties. The Senior Vice President, Business Operations and Chief Financial Officer, is a highly visible position which reports directly to the Chief Executive Officer. As Senior Vice President, Business Operations, you will be. responsible for developing and executing the business partnering strategy, inlicensing new technology and financial stewardship of the Company and such other duties and responsibilities as may be assigned to you from time to time by the Company's Chief Executive Officer. In this role, you will establish strategic alliances, lead the negotiation process and manage the process of developing new alliances. As Chief Financial Officer, you will be responsible for financial planning and accounting, SEC reporting, and financing of the Company. As part of these responsibilities, Finance, Operations, and Investor Relations/Public Relations will report directly to you.

The Senior Vice President/CFO is a member of the Company's Operating Committee and is critical to the Company maintaining a strong financial structure.

3. Salary and Bonuses.

a. Your base salary will be $7307.69 biweekly ($190,000 per year), subject to review and adjustment from time to time by the Board, in its sole discretion. Your base salary, as from time to time adjusted, is referred to in this letter as your "Base Salary." In addition to

Base Salary, you will be eligible to participate in the senior management bonus plan, with a target bonus of 15% of your Base Salary. Your 1997 bonus will be paid by the first payroll in January 1998 and will be 15% of your 1997 CytoTherapeutics' compensation. Bonus payments in future years will be based on achievement of Company and individual goals and are determined from time to time by the Board in its sole discretion.

4. Relocation. CytoTherapeutics will assist you with your relocation from Westborough to the Providence area, as per the attached Relocation Agreement, with the following two exceptions: 1) Since your "new" commute from your residence in Westborough does not meet the Federal IRS relocation rule for qualifying relocations, your relocation expenses will qualify for tax adder treatment as discussed in Paragraph 4 of the Relocation Agreement with a cap of $10,000 and, 2) the move can occur within 24 months of the starting date instead of within 12 months.

In addition to the provisions of this policy, the Company will pay any reasonable real estate commissions and closing costs incurred in connection with the sale of your present home and loan origination fees and other reasonable costs regarding the purchase of a new home (as specified in Addendum to the Relocation Agreement). All expenses must be approved in advance by the Head of Human Resources, and receipts must accompany the reimbursement request.

5. Stock Options. Through the Company's Stock Option Plan (a copy of which is attached), and subject to the terms and conditions of such Plan, you will receive options to acquire 130,000 shares of common stock of the Company (the "Option Shares"), subject to Board approval. We will issue as many of your options as Incentive Stock Options (ISOs) as is permitted by the Internal Revenue Code; the remaining options will be issued as Non-Qualified Options; in each case at an exercise price equal to the closing sale price on the Starting Date. Absent a change of control in the first two years of your employment, vesting for stock options will be based on continued employment as follows: (i) there will be no vesting during the first twelve months; (ii) options to acquire 32,500 Option Shares will vest on the first anniversary of your Starting Date; and (iii) 1/48th of Option Shares will vest each month thereafter for the next 36 months.

6. Benefits. You will be entitled to participate in any or all employee benefit plans, medical and dental insurance plans, life insurance, disability income plans, savings plans and other benefit plans from time to time in effect for senior management of the Company generally, except to the extent that such plans are duplicative of benefits otherwise provided to you under this Agreement. Such participation shall be subject to (i) the terms of the applicable plan documents, (ii) generally applicable policies of the Company and (iii) the discretion of the Board of Directors or any administrative or other committee provided for in or contemplated by such plan.

7. Confidentiality and Restricted Activities. You agree that some restrictions on your activities during and after employment are necessary to protect the goodwill, Confidential Information (as defined below) and other legitimate interests of the Company:

a. During your employment and thereafter, except as required by applicable law or for the proper performance of your duties and responsibilities hereunder, you shall not disclose to any person outside the company, corporation or other entity, or use for your own benefit or gain or otherwise, any Confidential Information. You understand that this restriction shall continue to apply after your employment terminates, regardless of the reason for such termination.

b. While you are employed by the Company and for a period of one (1) year thereafter you shall not, directly or indirectly, engage in any activity, whether as owner, partner, investor, consultant, employee, agent or otherwise, that is competitive with the business of the Company.

c. You further agree that during your employment and for one (1) year thereafter, you will not, directly or indirectly, attempt to hire any employee of the Company, assist in such hiring by any other person, corporation or entity, otherwise solicit, induce or encourage any employee of the Company to terminate his or her relationship with the Company.

d. You agree that you will not, during your employment with the Company, improperly use or disclose any proprietary information or trade secrets of any former or concurrent employer, or other person or entity with whom you have an agreement or duty to keep in confidence information acquired by you in confidence, if any; and that you will not bring onto Company premises any unpublished document or proprietary information belonging to any such employer, person or entity, unless consented to in writing by such employer, person or entity.

e. At the time of leaving the Company's employ, you will deliver to the Company (and not keep in your possession or deliver to anyone else) any and all devices, records, data, notes, reports, proposals, lists, employee lists, organization charts, correspondence, specifications, drawings, blueprints, sketches, materials, equipment, other documents or property, or reproductions of any aforementioned items developed or obtained by you pursuant to your employment with the Company, or otherwise belonging to the Company, its successors or assigns, or containing or constituting Confidential Information.

f. You agree that the Company shall, in addition to any other remedies available to it, be entitled to preliminary and permanent injunctive relief against any breach by you of the covenants contained in this Paragraph 7, without having to post bond. In the event that any provisions of this Paragraph shall be determined by any court of competent jurisdiction to be unenforceable by reason of its being extended over too great a time, too large a geographic

area or too great a range of activities, it shall be interpreted to extend only over the maximum period of time, geographic area or range of activities as to which it may be enforceable.

g. For purposes of this Agreement:

i. A business shall be deemed to be competitive with the Company if it engages or proposes to engage in any business activity (i) utilizing or seeking to develop technology capable of utilizing the transplantation of cells as a therapeutic agent for the diagnosis, prevention or treatment of human disease, injury or condition or (ii) in any field the Company is currently pursuing or has pursued within the previous two years.

ii. Confidential Information means any and all information of whatever type (including, without limitation, data, results, inventions, technology and all other information) of or relating to the Company including, without limitation, information relating to (1) the development, research, testing, production and marketing activities of the Company, (2) the Company's employees, consultants and other agents, (3) the products and services of the Company, (4) patients and clinical trials, (5) the costs, sources of supply and strategic plans of the Company, (6) the identity and special needs of the customers of the Company, (7) patents, trade secrets and other intellectual property and (8) people and organizations with whom the Company has business relationships and those relationships. Confidential Information also includes comparable information that the Company has received or may receive in the future of or relating to third parties where the Company has a duty to keep such information confidential. Confidential Information does not, however, include information that has become publicly known and generally available other than through a wrongful act by you.

8. Termination and Termination of Benefits. Your employment with the Company is "at will," which means that either you or the Company may terminate your employment at any time, with or without cause or good reason.

a. The Company may terminate your employment other than for "cause" at any time upon written notice to you and, in that event, (i) the Company will continue to pay you your Base Salary for the Severance Period (as defined below) or until you obtain other employment, whichever occurs first and (ii) all options which would have become vested during such Severance Period shall be treated as vested at the time of such termination. If, under these circumstances, you obtain other employment within the Severance Period, the Company will pay you the amount, if any, by which your prorated Base Salary exceeds your total compensation from your new employment for the remainder of the Severance Period. The Severance Period shall be nine months. Notwithstanding any other provision of this Agreement, if the value of your Option Compensation is greater than eight times your Base Salary, the Company shall have no obligation to continue to pay your Base Salary following your termination. Option Compensation shall mean an amount equal to the sum of the following (determined, in each case, by reference to the last closing sale price of the Company's Common Stock on the day prior to the date of your termination and including

options awarded to you by the Company pursuant to this Agreement or otherwise): (i) the aggregate difference between the value and exercise price of your vested but unexercised in-the-money stock options; (ii) the market value of any stock of the Company obtained by you on exercise of your stock options and still held by you, less the aggregate exercise price paid by you to obtain such stock; and (iii) the proceeds realized by you on the sale of any stock obtained by you on exercise of your stock options, less the aggregate exercise price paid by you to obtain such stock. In the event that you purchase stock from the Company (other than through the Company's Employee Stock Purchase Plan, the Company's 401(k) plan or as part of and on the same terms as a public or private offering of securities to investors) or are granted stock by the Company, Option Compensation shall also include (i) an amount equal to the market value of any such stock still owned by you, less the amount paid by you for such stock and (ii) the amount realized by you on the sale of any such stock sold by you, less the amount paid by you for such stock. Stock options will not continue to vest after your termination in the event of a resignation without good reason or termination with cause.

b. The Company may terminate your employment upon written notice to you in the event that you become disabled during your employment through any illness, injury, accident or condition of either physical or psychological nature and, as a result, you are unable to perform substantially all of your duties and responsibilities hereunder for ninety (90) days during any period of three hundred and sixty-five calendar days. In that event, the Company will continue to pay you your Base Salary until: (i) the end of a period of nine (9) months following such termination; (ii) you obtain other employment; or (iii) you become eligible for disability income under any disability income plan provided by the Company, whichever of these events shall occur first.

c. The Company may terminate your employment hereunder for cause at any time upon written notice to you setting forth in reasonable detail the nature of such cause. The following as determined by the Company in its reasonable judgment, shall constitute "cause" for termination:

(1) Your failure to perform, or material negligence in the performance of, (i) your principal duties and responsibilities to the Company (which, to the extent assigned to you, shall include those duties and responsibilities described in Paragraph numbered 2) or (ii) any other of your duties and responsibilities following written notice from the Company and a 10-business day opportunity to cure any curable failure or negligence;

(2) Any misconduct by you which is substantially injurious to the business or interests of the Company;

(3) Your violation of any federal, state or local law, regulation or other requirement applicable to the business of the Company;

(4) Your conviction or plea of "no contest" to, any felony; or

(5) Any material breach by you of any provision of this Agreement.

d. You may terminate your employment at any time, with or without good reason, upon written notice to the Company. If you terminate your employment with good reason, the Company will be obligated to you to the same extent as if the Company had terminated your employment other than for cause, and the Provisions of Paragraph 8 (a), including the acceleration of option vesting and the limitations on the Company's obligations contained therein, shall apply. The following shall constitute "good reason" for termination: material breach by the Company of any provision of this Agreement which breach continues for more than ten (10) business days following written notice from you to the Company setting forth in reasonable detail the nature of such breach.

e. If you resign other than for good reason or your employment is terminated by the Company for cause, the Company shall have no further obligation to you other than for Base Salary earned through the date of termination. No severance pay or other benefits of any kind will be provided.

f. In the event of a change of control (as defined in the Severance Practice; Change of Control Policy (10/94) (attached)) where CytoTherapeutics is not the surviving entity and the change of control results in a material change in job responsibility, compensation, or loss of job within the first two years of your employment with the Company, your severance will be the greater of the severance as defined in Paragraph 8(a) or the Severance Policy dated (10/94). In addition, if such material change resulting from a Change of Control occurs within the first two years of your employment, the options for 130,000 Option Shares granted to you with this offer shall vest fully upon such material change.

g. In the event we hire a new CEO, and that hiring results in a material change in your job responsibility, compensation, or loss of your job within the first two years of your employment with the Company, your severance will be as defined in Paragraph 8(a). In addition, if such material change resulting from a new CEO occurs within the first two years of your employment, the options for 130,000 Option Shares granted to you with this offer shall vest fully upon such material change.

9. Withholding. All payments and reimbursements made by the Company under this Agreement shall be reduced by any tax or other amounts required to be withheld by the Company under applicable law.

10. Assignment. This Agreement shall inure to the benefit of the Company and any successor of the Company by reorganization, merger, consolidation or liquidation and any assignee of all or substantially all of the business or assets of the Company or any division or line of business of the Company with which you are associated. The Company requires your personal services and you may not assign this Agreement.

11. Waiver. Except as otherwise expressly provided in this Agreement, no waiver of any provision hereof shall be effective unless made in writing and signed by the waiving party. The failure of either party to require performance of any term or obligation of this Agreement, or the waiver by either party of any breach of this Agreement, shall not prevent any subsequent enforcement of such term or obligation or be deemed a waiver of any subsequent breach.

12. Severability. Should any provision of this Agreement, or portion thereof, be found invalid in any circumstance, such invalidity shall not affect any other provision or circumstance, and such provision shall be construed by limiting it so as to be enforceable to the maximum extent compatible with applicable law.

13. Notices. Any notices, requests, demands and other communications provided for by this Agreement shall be in writing and shall be effective when delivered in person or five days after deposit in the United States mail, postage prepaid, registered or certified, and addressed to you at your last known address on the books of the Company or, in the case of the Company, at its main office, attention of the Chief Executive Officer.

14. Captions. The captions and headings in this Agreement are for convenience only and in no way define or describe the scope or content of any provision of this Agreement.

15. Entire Agreement. This Agreement sets forth the entire agreement and understanding between you and the Company and supersedes all prior communications, agreements and understandings, written and oral, with respect to the terms and conditions of your employment. This Agreement may not be changed or modified except by an agreement in writing signed by you and the Chief Executive Officer or other specifically authorized representative of the Company.

16. Governing Law. This Agreement shall be governed, construed and enforced in accordance with the laws of Rhode Island, without regard to principles of conflicts of law.

17. No Conflicting Agreements. You hereby represent to the Company that neither your execution and delivery of this Agreement nor your acceptance of employment with the Company nor your anticipated service as Senior Vice President, Operations and Chief Financial Officer will conflict with or result in a breach of any of the terms, conditions or provisions of any agreement to which you are a party or any order, injunction, judgment or decree of any court or governmental authority or any court or governmental authority or any arbitration award applicable to you.

18. Inventions. You hereby represent to the Company and agree that, except as described on Exhibit A, you have no inventions, original works of authorship, developments, improvements or trade secrets that were made by you prior to your employment with the Company and which relate to the Company's current or proposed business, products, or research and development. You will promptly make full written disclosure to the Company,

hold in trust for the Company's sole right and benefit, and hereby assign to the Company or its designee, all of your right, title and interest in any and all inventions, original works of authorship, developments, concepts, improvements or trade secrets, whether or not patentable or registerable under copyright or similar laws, that you may solely or jointly conceive, develop, reduce to practice or cause to be conceived or developed, or reduced to practice, during the period of time you are employed by the Company (collectively referred to as the "Inventions"). You further acknowledge that all original works of authorship made by you solely or jointly with others within the scope of your employment and protectible by copyright are "works made for hire", as that term is defined in the United States Copyright Act. You agree to keep and maintain adequate and current records of all inventions made by you solely or jointly with others during the term of your employment with the Company. Such records will be in the form of notes, sketches, drawings or any other format that may be specified by the Company. These records will be available through, and remain the sole property of, the Company at all times. You agree to assist the Company or its designee, at the Company's expense, in every proper way, to secure the Company's rights in the Inventions and copyrights, including the disclosure to the Company of all pertinent information and data with respect thereto, the execution of all applications, specifications, oaths, assignments and all other instruments that the Company shall deem necessary in order to apply for and obtain such rights, and in order to assign and convey to the Company, its successors, designees and nominees the sole and exclusive right, title, and interest in and to such Inventions, and any copyrights, patents, or other intellectual property rights relating thereto, both during your employment by the Company and thereafter. In the event that the Company is unable for any reason to secure or to prosecute any patent application with respect to such Invention (including, without limitation, renewals, extensions, continuations, divisions or continuations in part thereof), you hereby irrevocably designate and appoint the Company and its duly authorized officers and agents, as your agents and attorney-in-fact to act for and in your behalf and instead of you, to execute and file any such application and to do all other lawfully permitted acts to further the prosecution and issuance of patents thereon with the same legal force and effect as if executed by you. You agree that you will assist the Company in the prosecution and enforcement of the Company's intellectual property after termination of your employment, at the Company's expense.

19. Physical Exam. This offer of employment is contingent upon successful completion of a medical examination and a drug screen test which will be paid for by CytoTherapeutics. You will begin employment only after successfully passing both the medical exam and drug screen test. The results are generally available within 72 hours and you will be notified of the results.

20. Verification of Employment Eligibility. The Immigration Reform and Control Act of 1986 requires employers to verify the identity/employment eligibility of each employee hired after November 6, 1986. As a result, you will be asked to complete the attached Employment Eligibility Verification (Form I-9) on your first day of work. Section 2 of this form lists the documents you will be required to present.

21. Compliance With Agreement. The Company's obligations under this Agreement and its obligation to deliver stock under the terms of the stock options granted pursuant to the terms of this Agreement (or otherwise granted to you during the course of your employment) are conditioned on your compliance with the terms and conditions of this Agreement and the accuracy of the representations made to the Company by you herein.

If the foregoing is acceptable to you, please sign the enclosed copy of this letter in the space provided below and return it to me, whereupon this letter and such copy will constitute a binding agreement between you and the Company on the basis set forth above as of the date of the first above written.

Sincerely yours,

CYTOTHERAPEUTICS, INC.

By:/s/ Denise M. Peppard

Denise M. Peppard
Vice President, Human Resources

Accepted and agreed:

/s/ John McBride
- ---
John McBride

Date: 4/28/97

Enclosures:

Stock Option Plan Document/ Prospectus
Change of Control Policy
Relocation Policy and Addendum
Benefits Summary
Physical Exam form
Exhibit A - List of Prior Inventions
I-9 Form

EXHIBIT A

LIST OF PRIOR INVENTIONS & ORIGINAL WORKS OF AUTHORSHIP

Title	Date	Identifying Number or	Brief Description
None			

/s/ John S. McBride

Name of Employee (type or print)

CYTOTHERAPEUTICS, INC.
2 RICHMOND SQUARE
PROVIDENCE, RHODE ISLAND 02906

July 21, 1997

BY HAND DELIVERY

Sandra Nusinoff Lehrman, M.D.
c/o CytoTherapeutics, Inc.
2 Richmond Square
Providence, Rhode Island 02906

Dear Sandra:

As you know, CytoTherapeutics, Inc. (the "Company") is discussing several possible transactions, each of which (a "Transaction") would involve a material acquisition by the Company or the merger or affiliation of the Company or a subsidiary of the Company with another company. In addition, as we have also discussed, the Company believes that it may be necessary or desirable, whether in connection with a Transaction or in the absence of any Transaction, to effect certain changes in the Company's senior management, some of which changes we have, in fact, already accomplished.

In light of these developments, you and I have reviewed together your own role with the Company and we have determined that it is in our mutual best interests to effect a voluntary end to your employment with the Company, on the basis agreed to in this letter.

1. In signing this agreement, you resign your employment, and all offices and positions held by you, with the Company and its subsidiaries and other affiliates, including, without limitation, your position as a director of the Company, effective as of August 4, 1997 (the "Resignation Date"). It is understood and agreed that the Company will take actions in reliance on your resignation and that it is irrevocable.

2. During the period from the date of this letter, written above, through the Resignation Date (the "Transitional Period"), you will continue to be employed by the Company in your current position and at your current rate of pay. You need not report to the office on a daily basis during this period, but you do agree not to commence other employment during the Transitional Period and to remain available, during normal business hours, to provide advice and counseling to the Company, by telephone or at Company offices, as the Company may reasonably request. You also agree that, during the

Transitional Period and thereafter, you will not to attempt to bind the Company to the fulfillment of any condition, contract or obligation or to create any liability binding on the Company.

3. During the Transitional Period, the Company will continue your participation in those Company employee benefit plans in which you are currently a participant, to the extent permitted by the terms of those plans and generally applicable Company policies. Stock options granted you and not yet expired, exercised, canceled or otherwise become unexercisable shall continue to vest during the Transitional Period. In addition, subject to approval by the Company's Board of Directors, the exercise period for all of the options previously granted to you which shall have vested as of the Resignation Date shall be extended to the first anniversary of the Resignation Date ("Exercise Period Extension"), PROVIDED, HOWEVER, that all such options shall be exercisable only for so long as you continue to comply with your obligations under this agreement, including, without limitation, your obligations under paragraph 6 of this agreement. I will strongly recommend approval of the Exercise Period Extension at the August 4, 1997 meeting of the Board of Directors. In the unlikely event that the Board of Directors fails to approve the Exercise Period Extension at that meeting, the first Severance Period as defined in paragraph 4(a) will be extended for an additional three (3) months making a total Severance Period of nine (9) months.

4. In consideration of your acceptance of this agreement, and subject to your meeting all of your obligations under it, the Company will provide you the following:

(a) The Company will continue to pay you your salary, at your current base rate of pay, for a period of six (6) months (the "Severance Period") from the date of this letter, written above, reduced by the amount of any earnings you have from other employment following the Resignation Date. You agree to notify me immediately after obtaining any such employment and to provide accurate information concerning your compensation from such employment each pay period. Payments made to you hereunder after the Resignation Date shall continue to be made at the Company's regular payroll periods and in accordance with its usual payroll practices. In addition to the payments to be made to you hereunder after the Resignation Date you will be paid for all vacation that you may have earned but not used as of the Resignation Date.

(b) To the extent permitted by the terms of the Company's group health and dental plan and by its health and dental plan insurer or providers, as applicable, the Company will continue your participation and that of your eligible dependents (your husband and son) in its group health and dental plan to the same extent as you and they currently participate and will pay the premium cost of such participation, to the same extent currently paid, from the Resignation Date through the end of the Severance Period or the date you commence other employment and become eligible for coverage under the plans of

your new employer, whichever occurs first. If the Company is unable to provide the continuation as contemplated in the first sentence of this subsection (b), you may exercise your right to continue your coverage and that of your eligible dependents in the Company's group health and dental plan under the federal law known as COBRA, provided you are eligible to do so, and, if you are eligible and so elect, then, until the earlier of the end of the Severance Period or the date you cease to be eligible for continuation under COBRA, the Company will pay the premium cost of your coverage and that of your eligible dependents. The Company will also continue your coverage under its group life insurance plan in the same face amount in which your life is currently insured under such plan through the end of the Severance Period, or the date you commence other employment, whichever occurs first, provided such coverage is available under the plan. It is understood and agreed, however, that the benefits of the group health and group life insurance plans of the Company shall be subject to such conditions and limitations as are set forth in the applicable plan, policy or contract terms; that any disputes concerning eligibility for or payment of benefits under those plans shall be settled in accordance with the terms thereof; and that the Company shall have no liability to you, your dependents or anyone else claiming through you, for payment of benefits under any of such plan.

(c) The Company will reimburse your expenditures for outplacement services, to a maximum cost to the Company of Fifteen Thousand Dollars ($15,000).

(d) Promptly following the Resignation Date, the Company will provide you a positive written reference, signed by me, in the form attached hereto and marked "Exhibit A". In addition, I will respond personally to any inquiries made of the Company in a manner consistent with Exhibit A.

5. All payments by the Company under this agreement will be reduced by all taxes and other amounts that the Company is required to withhold under applicable law and all other deductions authorized by you.

6. Your obligations under Section 6 and Section 17 of the employment agreement between you and the Company dated July 2, 1996 (the "Employment Agreement") are incorporated into this agreement by reference and shall remain in full force and effect in accordance with their terms. You shall not be obliged to refund any of the bonus paid you pursuant to the first sentence of Section 3.b of the Employment Agreement.

7. You agree that you will not disclose this agreement or any of its terms or provisions, directly or by implication, except to members of your immediate family and to your legal and tax advisors, and then only on condition that they agree not to further disclose this agreement or any of its terms or provisions to others.

8. You agree that you will continue to use your best efforts to support and promote the interests and reputation of the Company during the Transitional Period. You agree that during the Transitional Period and thereafter, you will not disparage the Company or any of the people or organizations connected with it and that you will not otherwise do or say anything that could disrupt the good morale of the employees of the Company or otherwise harm its interests or reputation. Any representation made by you or on your behalf regarding your separation from the Company shall state that you resigned voluntarily and, if a Transaction shall occur or be announced by the Company on or before the Resignation Date, in connection with or in anticipation of such a Transaction or, if no such Transaction occurs or is so announced, in connection with a general management reorganization. You agree to make no statements inconsistent with the foregoing representation.

9. You agree to return to the Company, on the Resignation Date or such earlier date as the Company may specify, any and all documents, materials and information related to the Company's business, whether present or otherwise, and all keys and other property of the Company then in your possession or control.

10. In order to be certain that this agreement will resolve any and all concerns that you might have, the Company requests that you carefully consider its terms, including the release of claims set forth below and, in that regard, encourages you to seek the advice of an attorney before signing this agreement.

11. This letter contains the entire agreement between you and the Company and replaces all prior and contemporaneous agreements, communications and understandings, whether written or oral, with respect to your employment and its termination and all related matters, excluding only your obligations under Section 6 and Section 17 of the Employment Agreement and your obligations with respect to the securities of the Company.

12. In exchange for the Exercise Period Extension and the payments provided in paragraph 4(c), to which, you agree, you would not otherwise be entitled, you agree that this agreement shall be in complete and final settlement of any and all causes of action, rights or claims that you have had in the past, now have, or might now have, in any way related to, connected with or arising out of your employment or its termination or pursuant to Title VII of the Civil Rights Act, the Americans with Disabilities Act, the Age Discrimination in Employment Act, the Rhode Island fair employment practices statute or any other federal, state or local employment law, regulation or other requirement and you hereby release and forever discharge the Company, its subsidiaries and other affiliates and all of their respective past and present directors, shareholders, officers, employees, agents, successors and assigns and all others connected with them, both individually and in their official capacities, from any and all such causes of action, rights or claims.

13. In signing this agreement, you give the Company assurance that you have signed it voluntarily and with a full understanding of its terms and that you have had sufficient opportunity to consider this agreement and to consult with your attorney before signing it.

If the terms of this agreement are acceptable to you, please sign, date and return it to me within twenty-one days of the date you receive it. You may revoke this agreement at any time during the seven-day period immediately following the date of your signing by so notifying me in writing. If you do not do so, then, at the expiration of that seven-day period, this letter will take effect as a legally-binding agreement between you and the Company on the basis set forth above. The enclosed copy of this letter, which you should also sign and date, is for your records.

Sincerely,

CYTOTHERAPEUTICS, INC.

By: /s/ Seth A. Rudnick, President

Seth A. Rudnick, President

Accepted and agreed:

Signature: /s/ Sandra Nusinoff Lehrman

Sandra Nusinoff Lehrman

Date: July 21, 1997

Sandra Nusinoff Lehrman served as President and Chief Operating Officer of CytoTherapeutics, Inc. from July 1996 to August 1997. In addition, she served on the Board of Directors of the Company during that period. As Chief Operating Officer, all divisions of the Company's business reported to her, including finance and business, manufacturing, research, core technology, regulatory matters and human resources.

Dr. Lehrman's mission on her engagement as President and Chief Operating Officer was to coordinate and focus all functions of the Company during its critical period of transition from basic research to product development and commercial application. She accomplished that mission well, providing particularly strong leadership in defining critical path objectives for the Company's development programs in chronic pain, ALS, ophthalmology, among others. Dr. Lehrman's many talents include the ability to make the hard decisions necessary to advance the development of innovative pharmaceutical products and to manage the often complex process of obtaining critical regulatory approvals. During her tenure at the Company, Dr. Lehrman participated in the negotiation of significant alliances including the Company's alliance with Genentech. She brought a unique scientific depth and management breadth to the Company's product development and business operations.

Dr. Lehrman is a person of outstanding personal integrity. She is also a valued friend and colleague. I am grateful for the skill and leadership and talent she has given to the Company and its employees. We will miss her.

July 29, 1997

BY HAND DELIVERY

E. Edward Baetge, Ph.D.
c/o CytoTherapeutics, Inc.
Two Richmond Square
Providence, Rhode Island 02906

Dear Ed:

This letter will confirm the agreement reached between you and CytoTherapeutics, Inc. (the "Company) concerning your employment at the Company and the termination of such employment.

1. Your employment at the Company shall terminate effective on the earlier of October 24, 1997 or the date on which you start new full-time employment (the "Last Date"). (For purposes of this agreement, "full-time employment" shall mean provision of services on a full or substantially full-time basis, whether as an employee, consultant or otherwise, to an entity other than the Company.) In signing this agreement, you resign your position as Vice President, Research of the Company and all other officerships and directorships you hold with the Company or any of its subsidiaries or other affiliates, effective August 5, 1997, and your employment with the Company, effective as of the Last Date. During the remainder of your employment and thereafter, you shall not attempt to make any commitments on behalf of, or otherwise bind, the Company or any of its subsidiaries or other affiliates or cause any expenses to be incurred on their behalf. You will cease to represent yourself as an employee, agent or other representative of the Company as of the Last Date.

2. You will continue to receive your base salary on the Company's regular pay days through October 24, 1997. All requisite statutory withholdings and authorized deductions will be made from this pay. If you start new full-time employment, as defined above, you will cease to be an employee on such date and your salary payments will be discontinued as of the Last Date.

3. You have 168.71 hours of accrued unused vacation through the end of June 1997. You will receive a check for this vacation accrual on the Last Date. You will not continue to accrue additional vacation hours or other paid time off after June 30, 1997.

4. You may continue to participate in those Company employee benefit plans in which you are currently enrolled until the Last Date. Notwithstanding the foregoing, however, it is understood and agreed that your participation in any of the employee benefit plans of the Company shall be subject to such conditions and limitations as are set forth in the applicable plan, policy or contract terms; that any disputes concerning eligibility for or payment of benefits under those plans shall be settled in accordance with the terms thereof; and that the Company shall have no liability to you, your dependents or anyone else claiming through you, for payment of benefits under any of such plan. After the Last Date, you may elect to continue participation in the Company's group health and dental plans to the extent provided under COBRA. If you do so, then the Company will pay the premium cost of your participation from the Last Date until the earlier of the date you secure other employment or December 31, 1997. Thereafter, you may continue participation in the health and dental plans at your cost for any remainder of the COBRA period. Your participation in all other Company employee benefit plans will end as of the Last Date, in accordance with the terms of those plans.

5. The management shall recommend to its Board of Directors that all options granted you to purchase the Company's Common Stock which would be vested on December 18, 1997, and not yet exercised, expired, surrendered or canceled shall be fully vested on the Last Date and shall be exercisable for the shorter of the following two time periods: (i) nine months following the Last Date or (ii) six months from December 12, 1997. The foregoing is subject to the approval of the Board of Directors in its sole discretion. The management of the Company shall also recommend to its Board of Directors that the 500 shares of unvested restricted stock awarded to you on May 17, 1995 shall be vested on the Last Date. The foregoing is subject to the approval of the Board of Directors in its sole discretion. Except as otherwise expressly provided in this paragraph 5, all options granted you shall be pursuant to the terms of any applicable stock option certificate, agreement or plan and all options and restricted stock granted you shall be pursuant to any employee stock repurchase agreement or other restriction provisions generally applicable to shares purchased by Company employees and, in the case of the restricted stock, to all other applicable restrictions.

6. Nothing in this letter agreement is intended to alter or modify your right to any benefit to which you are entitled under the Company's 401(k) plan. Following the termination of your employment on the Last Date, you will receive information under separate cover concerning your 401(k) plan account and any distribution to you under that plan will be made in accordance with the terms of the plan. Any loans that you may have

against your 401(k) will need to be paid in full by the Last Date, pursuant to the terms of the 401(k) plan document.

7. Effective as of the close of business on the Last Date, your status as an employee of the Company shall cease for all purposes.

8. The agreement between you and the Company captioned Employment Agreement and signed by you on May 17, 1992 (the "Employment Agreement") shall remain in full force and effect in accordance with its terms, with your obligations under paragraphs 6 and 7 of the Employment Agreement with respect to solicitation of employees and covenants against competition continuing for a period of 12 months following the Last Date.

9. You and the Company shall be individually responsible for your and its attorneys' fees, if any, respectively.

10. No later than the Last Date, you will return to the Company all documents, files, books, keys, passes, identification materials, credit cards and other property of the Company.

11. You agree that you will not at any time disparage the Company or any of its subsidiaries or other affiliates or any of those associated with them and will take no steps and make no statements detrimental to the reputation of the Company or any of its subsidiaries or affiliates or any of those associated with them.

12. You agree to keep the terms of this letter agreement strictly confidential, and agree that you will not disclose, characterize, comment on, convey, or in any sense reveal the content or nature of this letter agreement, unless legally required to do so, to any persons other than your spouse, children or legal/tax/financial advisors, in which event you shall assure that your spouse, children and legal/tax/financial advisors shall be similarly bound by this covenant of confidentiality. The Company agrees to hold this letter agreement confidential and not reveal its terms except as its determines appropriate for business or legal reasons.

13. You agree to cooperate with the Company with respect to matters arising during or related to your employment, including but not limited to cooperation in connection with any litigation or governmental investigation or regulatory or other proceeding which may have arisen or which may arise following the execution of this letter agreement. As part of the cooperation agreed to herein, you shall provide complete and truthful information to the Company, its subsidiaries and other affiliates and their attorneys with respect to any matter arising during or related to your employment. Specifically, you shall make yourself available to meet with personnel and attorneys of the Company, its

subsidiaries and other affiliates and shall provide to them any and all documentary or other physical evidence pertinent to any such matter; and, at the Company's request upon reasonable notice, you shall travel to such places as the Company may specify (for which the Company will reimburse you for your reasonable travel and lodging expenses) and provide such complete and truthful information and evidence to parties whom the Company may specify. Further, upon the oral request of the Company or its attorneys, you shall testify, truthfully and accurately, to any such matter in any civil case to which the Company or any of its subsidiaries or other affiliates is a party or in connection with any investigation or regulatory or other proceeding relating to the Company or any of its subsidiaries or affiliates or their activities. Finally, you shall promptly notify the Company's General Counsel, within three business days, of your receipt from any third party or governmental entity of a request for testimony and/or documents, whether by legal process or otherwise, relating to any matter arising during or related to your employment.

14. This letter constitutes the entire agreement between you and the Company and supersedes all prior and contemporaneous agreements, communications and understandings, written and oral, with respect to your employment, its termination and all related matters, excluding only (a) the Employment Agreement, which shall remain in full force and effect in accordance with its terms, and (b) any obligations which you may have with respect to the securities of the Company or with respect to your loan under the 401(k) plan. In exchange for the special benefits provided to you under this agreement, you agree that this agreement shall be a complete and final settlement of, and releases the Company, its subsidiaries and other affiliates and all of their respective officers, directors, employees, shareholders, agents, successors and assigns (both individually and in their official capacities) from any and all causes of action, rights or claims that you have had in the past, now have, or might now have, in any way related to or arising out of your employment or its termination or pursuant to any federal, state or local employment laws, regulations or other requirements (including but not limited to causes of action or claims arising under Title VII of the Civil Rights Act of 1964, the Americans with Disabilities Act, the Age Discrimination in Employment Act and Rhode Island fair employment practices statute, each as amended).

15. All payments to be made to you in accordance with the terms of this letter agreement and the performance by the Company of any other obligations hereunder is conditioned upon your performance of your obligations hereunder and under the Employment Agreement.

16. The terms of this letter agreement shall be governed and construed in accordance with the laws of the State of Rhode Island, without regard to conflicts of laws rules thereof.

17. This letter agreement creates binding obligations and the Company therefore encourages you to seek the advice of an attorney before signing it. In signing this agreement, you give the Company assurance that you have signed it voluntarily and with a full understanding of its terms and that you have had sufficient opportunity to consider this agreement and to consult with your attorney before signing it and that you have done so.

If the foregoing is agreeable to you, please sign, date and return the enclosed copy of this letter to me no later than twenty-one (21) days after the date on which you received it. You may revoke this agreement within seven (7) days after you execute it and this agreement shall not become effective or enforceable until that revocation period has expired. If you do not revoke this agreement timely, then, at the expiration of that seven (7) day period, this letter and such copy shall take effect as a binding agreement between you and the Company on the basis set forth above.

Very truly yours,
CytoTherapeutics, Inc.

By: /s/ Frederic A. Eustis III

Title: Executive Vice President

Accepted and agreed:

/s/ E. Edward Baetge, Ph.D.

E. Edward Baetge, Ph.D.

Date: 8/4/97

LOAN AGREEMENT

THIS LOAN AGREEMENT, dated as of May 15,1996, is entered into by and between CytoTherapeutics, Inc., a Delaware corporation ("Borrower") and Fleet National Bank, a national banking association organized and existing under the laws of the United States of America ("Lender").

WHEREAS, Borrower desires to borrow funds from Lender in order to finance the purchase of certain equipment for use in its facilities; and

WHEREAS, Lender is willing to enter into such transactions on the terms and conditions hereinafter provided.

NOW THEREFORE, in consideration of the foregoing and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. DEFINITIONS

When used herein, the terms set forth below shall be defined as follows:

1.1 "Advance(s)" means advances of the Loan made by Lender to Borrower pursuant Section 3.1 hereof.

1.2 "Approved Lien" means any Lien, on any property of Borrower that: (a) Lender has consented to in writing; or (b) is listed on Exhibit D annexed hereto and made a part hereof.

1.3 "Authorized Investment Vehicles" means those investments permitted by the Policy.'Borrower's Address" means Two Richmond Square, Providence, Rhode Island 02906.

1.4 "Borrowing Limit" means the Two Million ($2,000,000) Dollars.

1.5 "Borrowing Request" means a request made by the Borrower for an Advance.

1.6 "Business Day" means any day which is not a Saturday or a Sunday and on which banks in the State of Rhode Island are not authorized to open or required to close.

1.7 "Cash Equivalents" means (a) Negotiable certificates of deposit and bankers' acceptances, maturing in one hundred eighty (180) days or less from the date of issue, or demand deposit or money market accounts, with any commercial bank or trust company which is organized under the laws of the United States or of any state there of and which has, or which his owned by a bank holding company which has, total assets in excess of $1,000,000,000; (b) any securities (i) which are commonly known as "commercial paper", (ii) which are due and payable within two hundred seventy (270) days from the date of issue, (iii) which have been issued by any corporation organized under the laws of the United States or of any state thereof or issued by a foreign corporation if such securities are denominated in United States dollars, and (iv) the rating for which, at the time of the acquisition thereof by the Borrower are not less than T-1" if rated by Moody's Investors Services, Inc., and not less than "A-1" if rated by Standard and Poor's Corporation; (c) any marketable direct or unconditionally guaranteed obligations of the United States of America or any agency thereof which mature within one (1) year from the date of the acquisition thereof; and (d) Authorized Investment Vehicles.

1.8 "Closing Date" means any day on which Lender makes an Advance to Borrower.

1.9 "Conversion Date" means that date which is one (l) year following the Date of Agreement.

1.10 "Date of Agreement" means May 15, 1996.

1.11 "ERISA" means, at any date, the Employment Retirement income Security Act of 1974 and the regulations thereunder, all as the same shall be in effect at such date.

1.12 "Equipment" shall have the meaning set forth in the Security Agreement.

1.13 "Event of Default" means each and every event specified in Section 6 of this Agreement.

1.14 "Financial Statements" means the balance sheet of Borrower, income statement of Borrower, and retained earnings statement of Borrower for the year or other period then ended, prepared in accordance with generally accepted accounting principles consistently applied and, in the case of the balance sheet, income statement, retained earnings statement and cash flow statement, as at the close of and for the fiscal year of Borrower, certified by Borrower's independent certified public accountants, and any supporting schedules and the notes to such financial statements.

1.15 "Indebtedness" means all obligations, contingent and otherwise, that in accordance with generally accepted accounting principles should be classified upon Borrower's balance sheet as liabilities, or to which reference should be made by footnotes thereto, including thereto, including in any event and whether or not so classified; (a) all debt and similar monetary obligations, whether direct or indirect; (b) all liabilities secured by any mortgage, pledge, security interest, lien, charge or other encumbrance existing on property owned or acquired subject thereto, whether or not the liability secured thereby shall have been assumed; and (c) all guarantees, endorsements and other contingent obligations whether direct or indirect in respect of indebtedness of others, including any obligation to supply funds to or in any manner to invest in, directly or indirectly, the debtor, to purchase indebtedness, or to assure the owner of indebtedness against loss, through an agreement to purchase goods, supplies, or services for the purpose of enabling the debtor to make payment of the indebtedness held by such owner or otherwise, and the obligations to reimburse the issuer in respect of any letters of credit.

1.16 "Lender's Address" is: 111 Westminster Street, Providence, Rhode Island 02903, Attn: Virginia C. Roberts, Senior Vice President.

1.17 "Lien" means any encumbrance, mortgage, pledge, hypothecation, charge, restriction or other security interest of any kind securing any obligation of any entity or person.

1.18 "Loans" means and includes all Advances made by Lender to Borrower pursuant to and payable in accordance with Section 3.1 hereof.

1.19 "Note" means that certain Note of Borrower in favor of Lender dated the Date of Agreement evidencing the Loans in the maximum principal amount of Two Million Dollars ($2,000,000.00) in the form attached hereto and made a part hereof as Exhibit A, together with all attachments thereto, as the same may be amended from time to time.

1.20 "Obligations" means all indebtedness, obligations and liabilities of Borrower to Lender, of every kind and description, direct or indirect, secured or unsecured, joint or several, absolute or contingent, due or to become due, whether for payment or performance, now existing or hereafter arising under or in connection with this Agreement, the Note, the Security Documents or in any other document or instrument delivered herewith or therewith or pursuant to the terms hereof or thereof, regardless of how the same may be evidenced, or whether evidenced by any instrument, agreement or book account, including, without limitation, all Loans, and all interest, taxes, fees, charges, expenses and attorneys' fees chargeable to Borrower pursuant to the terms hereof or of the Security Documents.

1.21 "Policy" means Borrower's Investment Policy, a copy of which is annexed hereto as Exhibit E.

1.22 "Premises" means any real estate owned, use or leased by Borrower including, without limitation, Borrower's Address.

1.23 "Security Agreement" means that certain Security Agreement by and between Borrower and Lender of even date herewith, as the same may be amended from time to time.

1.24 "Security Documents" means those instruments, agreements, documents and other writings executed by Borrower and listed on Exhibit C attached hereto and made a part hereof, together with any instruments, agreements, documents and other writings executed by Borrower (or Lender as Borrower's attorney in fact) in connection therewith.

1.25 "Tangible Net Worth" means at any time the excess of Borrower's total assets over its total liabilities at such time computed in accordance with generally accepted accounting principles consistently applied, less all of its intangible assets and deferred charges at such time, including, without limitation, goodwill, debt discount, organization expenses, trademarks and trade names, patents, deferred product development costs and similar items, also so computed.

1.26 "Unrestricted Liquidity" means at any time the sum of (a) Borrower's cash held in demand deposit accounts or interest bearing accounts at any financial institution plus (b) Cash Equivalents.

To the extent not defined in Section 1, unless the context otherwise requires, (a) all commercial terms not defined herein and defined in the Uniform Commercial Code as enacted in the State of Rhode Island on the Date of Agreement (the "Commercial Code") shall have the meanings set forth in the Commercial Code; and (b) all accounting terms not defined herein shall be defined, determined and calculated in accordance with generally accepted accounting principles, consistently applied and as applied in connection with and at the time of the preparation of the financial statements required under SECTION 5 hereof.

2. REPRESENTATIONS AND WARRANTIES

In order to induce Lender to enter into this Agreement and to make Advances to Borrower hereunder, Borrower represents and warrants to Lender, and such representations and warranties shall be continuing representations and warranties during the term of this Agreement and so long thereafter as any Obligations shall remain outstanding and shall be deemed repeated and confirmed at the time of each Closing Date as follows:

2.1 Borrower (a) is duly organized, validly existing and in good standing under the laws of the State of Delaware and has qualified to do business in the State of Rhode Island and is in good standing in that State.; (b) has and will have full power and authority to own its properties and to carry on business as now being conducted and is and will remain qualified to do business in every jurisdiction where such qualification is necessary and where failure to be so qualified would have a material adverse effect on the business of Borrower; and (c) has full power to execute, deliver and perform this Agreement and the Security Documents.

2.2 The execution, delivery and performance by Borrower of the terms and provisions of this Agreement, the Security Documents or any documents contemplated hereby: (a) have been duly authorized by all requisite corporate action; (b) do not violate any provision of law, any order of any court or other agency of government, the corporate charter or by-laws of Borrower; (c) will not violate any indenture, agreement or other instrument to which Borrower is a party, or by which Borrower or its assets is or are bound, or be in conflict with, result in a breach of, or constitute (with notice or lapse of time or both) a default under any such indenture agreement or instrument; and (d) will not result in the creation or imposition of any Lien, charge or encumbrance of any nature whatsoever upon any of the property or assets of Borrower pursuant to such indenture, agreement or instrument.

2.3 There is no action, suit or proceeding at law or in equity or by or before any governmental instrumentality or other agency now pending or, to the knowledge of Borrower, threatened, against or affecting Borrower which, if adversely determined, could have a material adverse effect on the business, properties, assets, liabilities, operations, results of operations, or condition, financial or otherwise, of Borrower.

2.4 Borrower is not a party to any agreement or instrument or subject to any charter or other corporate restriction adversely affecting its business, properties, assets, liabilities, operations, results of operations, or condition, financial or otherwise of Borrower.

2.5 Borrower is not in default in the performance, observance or fulfillment of any material of obligation, covenantor condition contained in any agreement or instrument to which it is a party.

2.6 No financing statement or agreement is on file in any public office pertaining to or affecting any property of Borrower, now owned or hereafter acquired, except as specifically set forth on Exhibit D attached hereto and made a part hereof.

2.7 Except for Approved Liens and liens permitted by Section 5.12, Borrower has good title to all of its properties and assets, free and clear of all mortgages, security interests, restrictions, Liens and encumbrances of any kind.

2.8 No statement of fact made by or on behalf of Borrower in this Agreement, or any Security Document, or in any certificate or schedule furnished to Lender pursuant hereto, or thereto contains any untrue statement of a material fact or omits to state any material fact necessary to make statements contained therein or herein not misleading. There is no fact presently known to Borrower which has not been disclosed to Lender which materially affects adversely, nor as far as Borrower can reasonably foresee, will materially affect adversely the business, properties, assets, liabilities, operations, results of operations, prospects or condition, financial or otherwise, of Borrower.

2.9 Borrower has filed all federal, state and local tax returns required to be filed and has paid or made adequate provision for the payment of all federal, state and local taxes, charges and assessments.

2.10 This Agreement and, the Security Documents have been duly executed and delivered by Borrower and constitute legal, valid and binding obligations of Borrower, enforceable in accordance with their respective terms, except to the extent that enforcement thereof may be limited by applicable bankruptcy, insolvency, reorganization, moratorium or similar laws of general application relating to or affecting the enforcement of the rights of creditors or by equitable principles, whether enforcement is sought in equity or at law.

2.11 No Event of Default and no event which, with the passage of time or the giving of notice, or both, would become such an Event of Default, has occurred and is continuing.

2.12 No "prohibited transaction" or "accumulated funding deficiency" or "reportable event" has occurred with respect to any "single employer plan" of Borrower. Borrower has not received notice that any "multi-employer plan" as to which it or any "commonly controlled entity" would have liability if it or any "commonly controlled entity" were to withdraw therefrom, is in "reorganization" or "insolvent" (as each of the quoted terms is defined or used in ERISA and the Internal Revenue Code of 1986, as amended (the "Code")).

2.13 Borrower has heretofore furnished to Lender Borrower's Financial Statements for the period ending December 31, 1995, which Financial Statements fairly present the financial condition of Borrower as of their date, and the results of its operations for the year or other period then ended. Since December 31, 1995, there has been no material adverse change in the business, properties, assets, liabilities, operations, results of operations, prospects or condition, financial or otherwise, of Borrower;

2.14 Each of Borrower and, to the best knowledge of Borrower, any other person relating to the Premises is in compliance in all material respects with all applicable U.S. federal, state and local Environmental laws and regulations. Borrower is not in violation of any law, rule, regulation or determination of an arbitrator, court, or other governmental authority, in each case, applicable to or binding upon Borrower or affecting any of its property, and in each case, which would have a material adverse effect.

2.15 Borrower has furnished to Lender copies of all material collaborative agreements to which it is a party.

2.16 None of the Equipment is an addition to, substitution for or replacement of the property described on Financing Statement 600321 filed with the Rhode Island Secretary of State, September 9, 1992, listing Borrower as Debtor.

3. LOAN AND PAYMENT PROVISIONS

Following the execution and delivery of this Agreement, and subject to the terms and conditions precedent enumerated in this SECTION 3 and in SECTION 4 hereof, 'Lender agrees to make Advances to Borrower (the "Commitment"), as follows:

3.1 ADVANCES

3.1.1 Subject to the terms and conditions of this Agreement, and provided no Event of Default has occurred and is continuing, from the Date of Agreement to the Conversion Date, Lender agrees to make Advances to Borrower, pursuant in each case to a Borrowing Request, provided that: (a) the dollar amount of the Loans, giving effect to the Borrowing Request, does not exceed the Borrowing Limit; (b) the Borrowing Request shall be in a minimum amount of, and thereafter in multiples of, One Hundred Thousand Dollars ($100,000); (c) Borrower shall have delivered to Lender a complete and accurate description of the Equipment to be purchased with the proceeds of the Advance or the Equipment purchased by Borrower prior to the Advance the purchase price of which shall be in the amount of the Advance and which shall constitute reimbursement to Borrower for the purchase price thereof together with such UCC Financing Statements duly executed on behalf of Borrower as Lender shall require; and (d) the conditions set forth in this SECTION 3.1 and in SECTION 4 shall have been fulfilled. The date on which any Advance shall be made shall be deemed a Closing Date. Lender shall disburse any such Advance into the general account of Borrower with Lender and shall furnish Borrower with notice of the making of the Advance and its disbursement. Advances made under this SECTION 3.1 shall be evidenced by and be payable in accordance with the terms of the Note.

3.1.2 An Advance shall be made by Lender to Borrower upon telephonic request to credit an Advance to Borrower's general account with Lender. Such Borrowing Request shall be made by an officer of Borrower duly authorized by Borrower's board of directors and whose name, along with a certified copy of such resolutions, have been provided to Lender. Each such Borrowing Request shall be confirmed in writing by Lender's receipt, within two (2) Business Days thereafter, of a Request for Advance in the form of Exhibit B attached hereto and made a part hereof. Borrower shall file with Lender specimen signatures of each officer authorized to make a Borrowing Request.

3.2 NOTE

3.2.1 Lender shall enter as debits against the indebtedness evidenced by the Note, all Advances, interest, charges, expenses and other items properly chargeable with respect to the Advances hereunder; and shall enter as credits against the indebtedness evidenced by the Note all payments made by Borrower on account of such indebtedness.

3.2.2 Absent manifest error the aggregate unpaid amount of the Note set forth on the Lender's internal records shall be PRIMA FACIE evidence of the principal amount thereof owing and unpaid to the Lender. Such records and/or schedule with respect to the indebtedness due under the Note shall not impair Lender's rights hereunder or under the Note or limit or otherwise affect Borrower's obligation to repay the Obligations in accordance with this Agreement.

3.2.3 Upon the occurrence of and during the continuance of an Event of Default, Lender shall be under no further obligation to make any additional Advances to Borrower.

3.2.4 The aggregate outstanding principal balance of the Note from time to time shall bear interest at the rate set forth in the Note and shall be evidenced by and be repayable in accordance with the terms and provisions of the Note.

3.3 BUSINESS DAY. Whenever any payment to be made hereunder or under the Note shall become due and payable on a day which is not a Business Day, such payment may be made on the next succeeding Business Day and, in the case of any payment of principal, such extension of time shall in such case be included in computing interest on such payment.

3.4 RELIANCE ON NOTICE. Lender shall incur no liability to Borrower for relying in good faith and in a commercially reasonable manner on any telephonic or written notice including, without limitation, a Borrowing Request, that purports to be from Borrower.

3.5 REPAYMENT. All payments of principal, interest, fees and all other amounts payable under this Agreement and the Note shall be made to Lender at its Providence, Rhode Island office (or at such other place as Lender may from time to time in writing specify to Borrower) in lawful money of the United States of America and in immediately available funds at the place of payment. If any payment shall fall due on a day which is not a Business Day at the place of payment, payment shall be made on the next succeeding Business Day at such place of payment and interest shall be payable for such extended time. Payments shall be made no later than 2:30 p.m. Providence time at the place of payment on the due date and any payment received after 2:30 p.m. Providence time shall be deemed to be paid on the following Business Day.

4. CONDITIONS PRECEDENT TO THE INITIAL AND SUBSEQUENT ADVANCES

Borrower shall satisfy the following conditions prior to the making of the initial Advance and/or each subsequent Advance by Lender hereunder, as follows:

4.1 INITIAL ADVANCE. All of the representations and warranties of Borrower set forth in Section 2 hereof shall be true and correct in all material respects as of the date of the initial Advance; Borrower shall be in full compliance with the terms and conditions hereof and no Event of Default shall have occurred and be continuing; and, in addition, Borrower shall have delivered to Lender, all in form and substance satisfactory to Lender, each of the Security Documents, together with:

(a) A certificate of the Secretary of Borrower containing copies of resolutions of the Board of Directors of Borrower authorizing the execution, delivery and performance of this Agreement, any document or instrument to be delivered pursuant hereto or in connection herewith and the transactions contemplated herein and therein, and identifying the officer or officers authorized to execute this Agreement and such other documents and to make requests for loans hereunder, which certificate shall be dated and delivered on the Date of Agreement;

(b) A certificate of reasonably recent date of the Secretary of State of Delaware , together with certificates of qualification to do business in Rhode Island and a Certificate of the Secretary of the State of Rhode Island, certifying that Borrower is in good standing in such jurisdiction;

(c) A certificate of a duly authorized officer of Borrower to the effect that:

(i) There has been no material adverse change in the condition (financial or otherwise) operations, assets or liabilities of the Borrowers since the date of the most recent Financial Statements delivered to Lender;

(ii) There have been no material adverse change in the corporate, organizational or legal structure of Borrower since the date of the most recent Financial Statements delivered to Lender;

(iii) Borrower is in compliance in all material respects with all applicable foreign and U.S. federal, state and local laws and regulations, including all applicable environmental laws and regulations.

(d) A list of all Equipment to be purchased with the proceeds of the Advance (or the Equipment already purchased the purchase price of which shall be refunded to Borrower from the proceeds of the Advance) in form and substance satisfactory to Lender;

(e) Pro-forma income statements and balance sheets, prepared by the management of Borrower for the fiscal years 1996-2000 inclusive;

(f) Insurance certificates or other evidence satisfactory to Lender in its sole discretion that Borrower has maintained insurance on its assets of such types and in such amounts as shall be satisfactory to Lender;

(g) A legal opinion of Borrower's counsel in form and substance satisfactory to Lender; and

(h) Copies of all material collaborative agreements between Borrower and third parties which collaborative agreements shall be satisfactory to Lender in its sole discretion.

4.2 SUBSEQUENT ADVANCES

4.2.1 All representations and warranties contained herein or otherwise made to Lender in connection herewith, shall be true and correct in all material respects with the same effect as though such representations and warranties had been made on and as of the date of the Closing Date, except to the extent such representations and warranties expressly relate to an earlier date or except as previously disclosed in writing to and accepted by Lender.

4.2.2 There shall exist (a) no Event of Default and (b) no condition, event or act which, with the giving of notice or lapse of time, or both, would constitute an Event of Default.

4.2.3 There shall be delivered to Lender: (a) a certificate dated the Closing Date signed by an officer of Borrower certifying in such detail as Lender may request to the fulfillment of conditions specified in SECTION 4.1 (C). SECTION 4.2. 1. and SECTION 4.2-2, which certificate shall be in the form of the Request for Advance attached hereto and made a part hereof as EXHIBIT B; (b) a description of the Equipment to be purchased with the proceeds of the Advance in accordance with Section 3.1.1; (c), such other UCC-1 Financing Statements as shall be required with respect to the Equipment and (d) documents and instruments as Lender shall reasonably request.

5. AFFIRMATIVE AND NEGATIVE COVENANTS

Borrower covenants and agrees that, from the date hereof and until payment and performance in full of all obligations of Borrower hereunder,, Borrower shall:

5.1 Do or cause to be done all things necessary to preserve, renew and keep in full force and effect its corporate existence, rights, licenses, permits and franchises, and comply, in all material respects, with all laws and regulations applicable to it; at all times maintain, preserve and protect all franchises and trade names and preserve all the remainder of its property used or useful in the conduct of its business and keep the same in good repair, working order and condition, and from time to time, make, or cause to be made, all needful and proper repairs, renewals, replacements, betterments and improvements thereto, so that the business carried on in connection therewith may be properly conducted in a manner consistent with the ordinary course of business at all times.

5.2 Pay and discharge or cause to be paid and discharged all taxes, assessments and governmental charges or levies imposed upon it or upon its respective income and profits or upon, any of its property, real, personal or mixed, or upon any part thereof, before the same shall become in default, as well as all lawful claims for labor, materials and supplies or otherwise, which, if unpaid, might become a lien or charge upon such properties or any part therefor; provided that Borrower shall not be required to pay and discharge or cause to be paid and discharged any such tax, assessment, charge, levy or claim so long as the validity thereof shall be contested in good faith by appropriate proceedings and it shall have set aside on its books adequate reserves with respect to any such tax, assessment, charge, levy or claim, so contested, and provided, further, that payment with respect to any such tax, assessment, charge, levy or claim shall be made before any of its property shall be seized and/or sold in satisfaction thereof.

5.3 Give prompt written notice to Lender of any proceedings instituted against Borrower by or in any federal or state court or before any commission or other regulatory body, federal, state or local, which, if adversely determined, would have a materially adverse effect upon its business, operations, properties, assets, or condition, financial or otherwise.

5.4 Furnish to Lender:

(a) Within one hundred twenty (1 20) days after the end of each fiscal year, Financial Statements of Borrower certified by independent public accountants approved by Lender and showing its financial condition at the close of such fiscal year, the results of operations during such year together with a Certificate of Compliance regarding the financial covenants set forth in Sections 5.8 and 5.9;

(b) Within forty-five (45) days of the close of each of the first three (3) fiscal quarters of each fiscal year of Borrower, Financial Statements of the type specified in subsection (a) above, certified by the Chief Financial Officer of Borrower, together with a Certificate of Compliance regarding the financial covenants set forth in Sections 5.8 and 5.9;

(c) Within ten (10) days after their filing, any filing made with the Securities and Exchange Commission including, without limitation, Forms 1OK, 10Q and 8K and any proxy statements.

5.5 Promptly, from time to time, furnish such other information regarding Borrower's business, properties, assets, liabilities, operations, results of operations, prospects or condition; financial or otherwise, as Lender may reasonably request; and promptly advise Lender of any material adverse change in the Borrower's business, properties, assets, liabilities, operations, results of operations, prospects or condition, financial or otherwise, and of any condition or event which constitutes, or with notice or lapse of time or both would constitute, an Event of Default.

5.6 Permit agents or representatives of Lender at reasonable times, and upon reasonable notice if no Event of Default shall have occurred and without notice upon the occurrence and continuance of an Event of Default , to inspect Borrower's books and records and to make abstracts or reproductions of such books I and records, the cost of such inspections to be borne by Borrower.

5.7 Execute and deliver to Lender any financing statement, including any amendment or continuation statement, which Lender deems necessary to be executed, delivered or filed by Lender in connection with this Agreement or the Security Documents, and Borrower does hereby (a) make, constitute and appoint Lender or its agent its true and lawful attorney-in-fact, for, in its name and on its behalf to execute and deliver for filing any financing statement, including any amendment or continuation statement, which Lender or its agent deems necessary to be executed, delivered or filed by Lender in connection with this Agreement, (b) ratify and confirm all that said attorney-in-fact shall do or cause to be done by virtue of this paragraph, and (c) agree to take any and all actions and execute such other instruments as Lender may reasonable require.

5.8 Maintain at all times a ratio of its total liabilities to Tangible Net Worth not to exceed .5:1, such ratio to be determined in accordance with generally accepted accounting principles consistently applied.

5.9 Maintain at all times Unrestricted Liquidity in an amount equal to or in excess of Eleven Million Dollars ($1 1,000,000).

5.10 Maintain Lender as Borrower's principal bank of account.

5.11 Not create, incur or assume any Indebtedness other than (i) Indebtedness to Lender, (ii) Indebtedness in respect of the acquisition of property which does not exceed $500,000 in the aggregate, (iii) current liabilities of the Borrower not incurred through the borrowing of money or the obtaining of credit except credit on an open account customarily extended, (iv) Indebtedness in respect of taxes or other governmental charges contested in good faith and by appropriate proceedings and for which adequate reserves have been taken; and (v) Indebtedness not included above and listed on SCHEDULE 5.11 hereto;

5.12 Not create or incur any Liens on any property or assets of the Borrower except (i) Liens securing the Obligations; (ii) Liens securing taxes or other governmental charges not yet due; (iii) deposits or pledges made in connection with social security obligations; (iv) Liens of carriers, warehousemen,

mechanics and materialmen, less than 120 days old as to obligations not yet due; (v) easements, rights-of-way, zoning restrictions and similar minor Liens which individually and in the aggregate do not have a materially adverse effect; (vi) purchase money security interests in or purchase money mortgages on real or personal property securing purchase money indebtedness permitted by the preceding Section 5.1 1, covering only the property so acquired; and (vii) other Liens existing on the date hereof and listed on Exhibit D.

5.13 Not sell, lease, transfer or otherwise dispose of Borrower's properties, assets, rights, licenses or franchises to any person, or turn over the management of, or enter a management contract with respect to, such properties, assets, encumbrances or rights, licenses and franchises other than in the ordinary course of business.

5.14 Not dissolve, liquidate, consolidate with or merge with or otherwise acquire all or substantially all of the assets or properties of, any other person or business, or change the Borrower's corporate name.

5.15 Except for transactions listed on Schedule 5.20, not enter into any arrangement, directly or indirectly, with any person whereby Borrower shall sell or transfer any property, real, personal or mixed, used or useful in its business, whether now owned or hereafter acquired, and thereafter rent or lease such property.

5.16 Not purchase, invest in or otherwise acquire or hold securities, including without limitation, capital stock and evidences of indebtedness of, or make loans or advances to, or enter into any arrangement for the purpose of providing funds or credit to, any other person, except:

(a) investments made by Borrower pursuant to the Policy;

(b) investments in readily marketable short term direct obligations of the United State of America or United States federal government agencies or instrumentalities;

(c) certificates of deposit, time deposits or banker's acceptances issued by the Lender or any affiliate of the Lender or commercial banks of recognized standing organized and existing under the laws of the United States of America and having a commercial paper rating in one of the two highest categories of Standard & Poor's Corporation or Moody's Investor's Service Inc.; and

(d) such other investments as the Lender may from time to time approve in writing.

5.17 Not engage, directly or indirectly, in a business substantially different from the business now being conducted.

5.18 Maintain casualty insurance coverage on its physical assets and other insurance against other risks, including public liability and product liability insurance in such amounts and of such types as may be requested by Lender from time to time and, in any event, as are ordinarily carried by similar businesses; and, in the case of all policies insuring the Equipment, all such insurance policies shall provide that the proceeds thereof shall be payable to Borrower and Lender, as their respective interests may appear. Borrower has a right of free choice of agent and insurer through or by which such insurance is to be placed, subject only to the requirements that the insurer be authorized to do business in each state where its property and/or assets are located and have a licensed agent therein and that such insurer's financial condition is reasonably satisfactory to Lender. All said policies or certificates thereof, including all endorsements thereof and those required hereunder, shall be deposited with Lender; and such policies shall contain provisions that no such insurance may be canceled or decreased without thirty (30) days prior written notice to Lender If Borrower shall at any time or times hereafter fail to obtain and maintain any of the policies of insurance required herein, or fail to pay any premium in whole or in part relating to any such policies, Lender may, but shall not be obligated to, obtain and/or cause to be maintained insurance coverage with respect to the Equipment, including, at Lender's option, the coverage provided by all or any of the policies of Borrower and pay all or any part of the premiums thereunder, without waiving any Event of Default by Borrower, and any sums so disbursed by Lender shall be additional Obligations of Borrower

to Lender, payable on demand. Lender shall have the right to settle and compromise any and all claims under any of the policies required to be maintained by Borrower hereunder, to demand, receive and receipt for all monies payable thereunder, to execute in the name of Borrower or Lender or both any proof of loss, notice or other instruments in connection with such policies or any loss thereunder.

5.19 Not permit any pension plan maintained by Borrower or by any member of a "controlled group" (ERISA 21 0(c)) or "corporation or group of trades or businesses under common control" (ERISA 21 0(d)) of which Borrower is a member to: (a) engage in any "prohibited transaction" (ERISA 2003(c)); (b) fail to report to the Lender a "reportable event" (ERISA 4043) within thirty (30) days after its occurrence; (c) incur any "accumulated funding deficiency" (ERISA 302); or (d) terminate its existence at any time in a manner which could result in the imposition of a lien on the property of Borrower; or (e) fail to report to Borrower any "complete withdrawal" or "partial withdrawal" by Borrower or any affiliate from a "multi-employer plan" (ERISA 4203, 4205 and 4001 respectively) (the quoted terms are defined in the respective sections of ERISA cited above).

5.20 Not declare or pay any dividends, or make any distribution of cash or property, or both, to holders of shares of its capital stock, nor directly or indirectly redeem, purchase or otherwise acquire for a consideration any shares of its capital stock, of any class, provided, however, nothing in this Agreement shall affect Borrower's right to enter into the transactions described on Schedule 5.20.

5.21 Comply with all applicable laws and regulations, including all applicable environmental and securities laws, whether now in effect or hereafter enacted or promulgated by any governmental authority having jurisdiction in the premises.

5.22 Use any Advance solely for the purchase of Equipment (or to reimburse Borrower for the purchase price of Equipment a description of which has been furnished to Lender).

6. EVENTS OF DEFAULT AND ACCELERATION

6.1 The occurrence of any one or more of the following events shall constitute an Event of Default hereunder:

6.1.1 Default in the payment of any principal, interest or other charges in respect of any of the Obligations for a period of five (5) days after the same becomes due and payable;

6.1.2 Default in the observance or performance of any covenant or agreement of the Borrower herein set forth, or default in the observance or performance of any covenant or agreement of Borrower set forth in the Security Documents;

6.1.3 If any representation, warranty, certificate, schedule or other information made or furnished by Borrower herein or pursuant hereto is or shall be untrue or misleading in any material respect;

6.1.4 Borrower defaults, receives notice of default or notice of impending default with respect to any evidence of indebtedness, obligations or liabilities or other material agreement of Borrower (other than to Lender), if the effect of such default is to accelerate the maturity of such indebtedness or to permit the holders thereof (or any portion thereof) to cause such indebtedness to become due prior to the stated maturity thereof, or if any indebtedness of Borrower (other than to Lender), is not paid when due and payable, whether at the due date thereof or a date fixed for prepayment or otherwise;

6.1.5 The occurrence of any material loss, theft, damage or destruction of the property of Borrower, or the making of any levy, seizure or attachment by any third party upon any collateral for the Obligations hereunder;

6.1.6 Borrower shall (a) apply for, consent to, or suffer the appointment of a custodian, receiver, trustee or liquidator of it or any of its property, (b) file or suffer the filing of any voluntary or

involuntary petition under any chapter of the Bankruptcy Code by or against the Borrower, or (c) apply for or permit the appointment of a receiver, trustee or custodian of any of the property or business of the Borrower, or (d) become insolvent or suffer the entry of an order for relief under Title 1 1 of the United States Code, or (e) make an admission of its inability to pay its debts as they become due, and which, in the case of any involuntary proceeding under (a), (b), (c) or (d), is not dismissed or discharged within thirty (30) days of its commencement;

6.1.7 An order, judgment or decree shall be entered, without the application, approval or consent of Borrower by any court of competent jurisdiction, approving a petition seeking reorganization of Borrower or appointing a custodian, receiver, trustee or liquidator of Borrower or of all or a substantial part of the assets of Borrower;

6.1.8 Borrower discontinues or suspends or threatens to discontinue or suspend the operation of Borrowers business or a substantial part thereof (as presently conducted) for any reasons; or

6.1.9 The occurrence of any event of default or default under any Security Document or any other agreement by and between Borrower and Bank.

6.2 If any Event of Default shall occur, then or at any time thereafter, while such Event of Default shall continue, Lender may terminate this Agreement and declare all Obligations to be due and payable, without notice, protest, presentment or demand, all of which are hereby expressly waived by Borrower.

7. MISCELLANEOUS

7.1 Lender shall have, in addition to any other rights and remedies contained in this Agreement and the Security Documents, and any other agreements, guarantees, notes, instruments and documents heretofore, now or at any time or times hereafter executed by Borrower and delivered to Lender, all of the rights and remedies of a secured party under the Uniform Commercial Code in force in the State of Rhode Island, all of which rights and remedies shall be cumulative, and none exclusive, to the extent permitted by law.

7.2 No failure to exercise and no delay in exercising on the part of Lender, any right, power, privilege or remedy under this Agreement, shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or privilege hereunder preclude any other or further exercise thereof or the exercise of any other right, power or privilege. Every maker, endorser and guarantor of this Agreement waives presentment, demand, notice and protest and all defenses based on the giving of time and other indulgence, substitution, exchange, or release of collateral or release of any person primarily or secondarily liable thereunder.

7.3 Whether or not the financial accommodations provided for by this Agreement are made, Borrower agrees to pay, or reimburse Lender, for actual and reasonable out-of-pocket expenses, including counsel fees, reasonably incurred by Lender in connection with the development, preparation, execution, administration, collection or enforcement of or the preservation of any rights under this Agreement. This Section shall survive the payment of any amounts due in respect of the Revolving Note, this Agreement and the termination of this Agreement. Notwithstanding the generality of the foregoing, Borrower will defend, indemnify and hold harmless Lender, its employees, agents, officers and directors, from and against any and all reasonable claims, demands, penalties, causes of action, fines, liabilities, settlements, damages, penalties, costs or expenses of whatever kind or nature known or unknown, foreseen or unforeseen, contingent or otherwise arising out of any breach by Borrower of any of the provisions of this Agreement.

7.4 This Agreement shall be binding upon and inure to the benefit of Borrower and Lender and their respective successors and assigns, except that Borrower may not transfer or assign any of its rights hereunder without the prior written consent of Lender. Lender may transfer or assign all or part of its rights under this Agreement and sell participating interests therein at any time and from time to time. All

references to Lender herein or in any instrument delivered to Lender in connection herewith or therewith, shall be deemed to apply to any holder for the time being of the Revolving Note.

7.5 This Agreement and the rights and obligations of the parties hereunder shall be governed by, and construed and interpreted in accordance with the laws of the State of Rhode Island. The article and section headings used herein are solely for reference and shall not be used in the interpretation or the construction hereof.

7.6 No modification or waiver of any provision of the Revolving Note or of this Agreement and no consent by Lender to any departure therefrom by Borrower shall be effective unless such modification or waiver shall be in writing and signed by a duly authorized officer of Lender, and the same shall then be effective only for the period and on the conditions and for the specific instances and purposes specified in such writing. No notice to or demand on Borrower in any case shall entitle Borrower to any other or further notice or demand in similar or other circumstances.

7.7 BORROWER HEREBY EXPRESSLY WAIVES TRIAL BY JURY IN CONNECTION WITH ANY SUIT OR ACTION ARISING OUT OF OR CONCERNING ITS OBLIGATIONS IN CONNECTION WITH THIS AGREEMENT, THE NOTE OR ANY INSTRUMENT OR DOCUMENT DELIVERED PURSUANT TO THIS AGREEMENT.

7.8 Borrower hereby grants to Lender a continuing lien for all Obligations upon any and all monies, securities and other property of Borrower and the proceeds thereof, now or hereafter held or received by or in transit to, Lender from or for Borrower, whether for safekeeping, custody, pledge, transmission, collection or otherwise, and also upon any and all deposits (general or special) and credits of Borrower with, and any and all claims of Borrower against, Lender, at any time existing. Upon the occurrence and continuance of any Event of Default, Lender is hereby authorized at any time and from time to time, without notice to Borrower, to set off, appropriate and apply any or all items hereinabove referred to against all Obligations.

7.9 Borrower hereby submits to the jurisdiction of the courts of the State of Rhode Island and the United States District Court for the District of Rhode Island, as well as to the jurisdiction of all courts from which an appeal may be taken from the aforesaid courts for the purpose of any such suit, action or other proceeding arising out of the breach by Borrower of any of its obligations under and with respect to this Agreement, the Revolving Note or any instrument delivered pursuant to this Agreement and expressly waives any and all objections it may have as to venue in any of such courts and agrees that service of process may be made on Borrower by mailing a copy of the summons to Borrower's Address.

7.10 All covenants, agreements, representations and warranties made in this Agreement and in any certificates or schedules delivered pursuant hereto shall survive the making by Lender of the financial accommodations hereunder and shall continue in full force and effect until the Obligations are paid in full.

7.11 This Agreement may be executed by the parties hereto individually or in any combination, in one or more counterparts, each of which shall be an original and all of which shall together constitute one and the same Agreement.

7.12 If any provision of this Agreement shall be held to be invalid, illegal or unenforceable, the validity of all other terms hereof shall in no way be affected thereby.

7.13 All demands, notices and other communications hereunder shall be in writing, except as otherwise provided in this Agreement, and shall be sent to the other party by registered or certified mail, return receipt requested, by overnight delivery service, by telegraph, telecopier or facsimile, or by hand delivery, addressed:

(a) If to Borrower, to it at:

CytoTherapeutics, Inc.
Two Richmond Square
Providence, Rhode Island 02906
Attn: Daniel E. Geffken

with a copy to:

Ropes & Gray
One International Place
Boston, MA 02110-2624
Attn: Geoffrey B. Davis, Esq.

and

(b) If to Lender, to it at:
Fleet National Bank
111 Westminster Street
Providence, Rhode Island 02903
Attn: Virginia C. Roberts, Senior Vice President

with a copy to:

Adler Pollock & Sheehan Incorporated
2300 Hospital Trust Tower
Providence, Rhode Island 02903-2443
Attn: Sarah T. Dowling, Attorney

The address of any party for such demands, notices and other communications may be changed by giving notice in writing at any time to the other party hereto. Any demand, notice or other communication shall be deemed to have been given: (a) if sent by registered or certified mail, three (3) Business Days following deposit in the United States mail; (b) if sent by overnight delivery service, one (1) Business Day following delivery to the overnight delivery service; (c) if sent by telegraph, telecopier or facsimile, when receipt of such transmission is acknowledged; or (d) if sent by hand delivery, upon actual delivery.

IN WITNESS WHEREOF, the parties have executed this Loan Agreement the day and year first above written.

WITNESS: CytoTherapeutics, Inc.

By: /s/ DANIEL E. GEFFKEN

Daniel E. Geffken
VICE PRESIDENT/CHIEF FINANCIAL OFFICER

WITNESS:

Fleet National Bank

By: /s/ VIRGINIA C. ROBERTS

Virginia C. Roberts
SENIOR VICE PRESIDENT

EXHIBIT A

NOTE

$2,000,000 May 15, 1996

FOR VALUE RECEIVED, the undersigned CytoTherapeutics, Inc. a Delaware corporation ("Borrower"), unconditionally promises to pay to Fleet National Bank, a national banking association ("Lender"), or order, at its offices at 1 1 1 Westminster Street, Providence, Rhode Island, or at such other place as may be designated in writing by the holder hereof, in lawful money of the United States, the principal sum of Two Million Dollars ($2,000,000), or such lesser sum as may be outstanding pursuant to the terms hereof and pursuant to that certain Loan Agreement of even date herewith by and between Borrower and the Lender (hereinafter referred to as the "Loan Agreement"), together with interest in arrears from the date hereof on the unpaid principal balances hereunder at the rate of interest equal to (a) the rate of interest designated by Lender from time to time as being its prime rate of interest plus one half (1/2%) percent per annum ("Floating Rate") or (b) the Fixed Rate of Interest elected by Borrower and offered by Lender in accordance with the terms and provisions set forth on Exhibit A annexed hereto and made a part hereof.

As used herein,-the Prime Rate shall mean the rate of interest designated by Fleet National Bank, a national banking association, from time to time as being its prime rate of interest.

Interest shall be paid monthly commencing June 1, 996 and continuing on the same day of each successive month thereafter.

The outstanding principal balance hereunder on May , 1997 shall be paid in twelve (12) equal, consecutive quarterly installments of principal together with interest thereon commencing August 1, 1997 and continuing on the same day of each November, February, May and August thereafter with a final payment of the entire balance then remaining due under this Note on May 1, 2000. Each change in the Floating Rate resulting from a change in the Prime Rate shall become effective as of the opening of business on the day on which such change in such Prime Rate occurs. Interest shall be calculated in arrears on the basis of a three hundred and sixty (360) day year but shall accrue and be payable on the actual number of days elapsed.

In the event any payment hereunder is not paid in full when due, Obligors (as hereinafter defined) shall pay to Lender, to the extent permitted by law, a processing fee on such unpaid amount equal to five percent (5%) of such late payment.

All payments made in connection with this Note shall be applied first to interest then accrued and unpaid and the balance only to principal in inverse order of maturity.

Notwithstanding anything herein to the contrary, in no event shall the interest charged, reserved and/ or taken on the loan evidenced hereby exceed the maximum allowed by and determined in accordance with applicable law.

Borrower, any indorser hereof, any other party hereto and any guarantor hereof (collectively "Obligors") and each of them: (i) waive presentment, demand, notice of demand, protest, notice of protest and notice of nonpayment and any other notice required to be given under the law to any of Obligors, in connection with the delivery, acceptance, performance, default or enforcement of this Note, any endorsement or guaranty of this Note or any document or instrument evidencing any security for payment of this Note; (ii) consent to any and all delays, extensions, renewals or other modifications of this Note or waivers of any term hereof or release or discharge by Lender of any of Obligors or release, substitution or exchange of any security for the payment hereof or the failure to act on the part of Lender or any other indulgence shown by Lender, from time to time and in one or more instances (without notice to or further assent from any of Obligors) and agree that no such action, failure to act or failure to exercise any right or

remedy on the part of Lender shall in any way affect or impair the obligations of any Obligor or be construed as a waiver by Lender of, or otherwise affect, any of Lender's rights under this Note, under any endorsement or guaranty of this Note or under any document or instrument evidencing any security for payment of this Note; and (iii) jointly and severally agree to pay, on demand, all costs and expenses of collection of this Note or of any endorsement or any guaranty hereof and/or the enforcement of Lender's rights with respect to, or the administration, supervision, preservation, protection of, or realization upon, any property securing payment hereof, including reasonable attorneys' fees, and agree that Lender has a lien on, a continuing security interest in, and a right to set off at any time, without notice, with respect to all of the respective properties and deposit account of any of Obligors at, or under the control of, Lender, or any of its affiliates.

Whenever there is an Event of Default under the Loan Agreement, Lender shall have all the rights and remedies set forth therein and, in addition, the rate of interest due and payable hereunder shall, from and after such Event of Default, be equal to the then applicable interest rate plus three percent (3%) per annum (the "Default Rate").

This Note shall be governed by and construed in accordance with the laws of the State of Rhode Island, without reference to its conflict of laws principles. The term "Lender" shall include Lender's successors, indorsees and assigns.

This Note is the Note referred to in, and is entitled to the benefits of, the Loan Agreement. This Note is secured, inter alia, by the Security Agreement (as defined in the Loan Agreement) and is entitled to the benefits thereof.

IN THE PRESENCE OF:

CytoTherapeutics, Inc.
By:
Name:
Title:

EXHIBIT A

To Note
Dated May 15, 1996 of CytoTherapeutics ("Borrower")
in favor of Fleet National Bank, a national
banking association (together with any other
holder of the Note, the "Lender")

1. DEFINITIONS OF CERTAIN TERMS

As used in this Exhibit A to Note, the following terms shall have the following meanings (such meanings to be equally applicable to both the singular and plural forms of the terms defined):

"Business Day" means any day which is not Saturday or Sunday and on which banks in the State of Rhode Island are not authorized or required to close.

"Cost of Funds Rate" means the rate of interest which the Lender is required to pay (or offering to pay) on the date in question for such borrowing and obligations (such as $100,000 certificates of deposit) having a term equal to the applicable Fixed Rate Term, as the Lender, in its sole discretion, may deem appropriate, but adjusted for reserve requirements and such other requirements as may be imposed by federal, state and/or local government and regulatory agencies and for fees assessed by the Lender's Money Management Department.

"Dollars" and the sign I" mean lawful money of the United States of America.

"Fixed Rate" means with respect to any portion of the Loan constituting a Fixed Rate Loan, the Cost of Funds Rate plus three (3%) percent per annum.

"Fixed Rate Loan" means a Loan bearing interest at the Fixed Rate.

"Fixed Rate Term" has the meaning assigned thereto in paragraph 4(A), below.

"Floating Rate" shall have the meaning set forth in the Note.

"Interest Adjustment Date" means (i) as to any Prime Rate Loan, the Business Day elected by the Borrower in its applicable Interest Rate Election, but being no earlier than the Business Day of receipt by the Lender before 1:00 P.M. on a Business Day of an Interest Rate Election changing the interest rate on such Loan to the Fixed Rate; and (ii) as to any Fixed Rate Loan, the last Business Day of the Fixed Rate Term pertaining to such Fixed Rate Loan.

"Interest Rate Election" means Borrower's irrevocable telecopied or telephonic notice which in the case of telephonic notice shall be promptly confirmed by a written notice of election that the Floating Rate or the Fixed Rate shall apply to all or any portion of the Loans, which subject to this Note and the Loan Agreement, shall be effective on the next Interest Adjustment Date, such telecopied, telephonic or written notice and written confirmation thereof to be in the form of SCHEDULE 1,attached hereto and by this reference fully incorporated herein and to be received by the Lender prior to 1:00 P.M. on the Business Day on which such Interest Rate Election is to take effect, each such Interest Rate Election, subject to the terms of the Loan Agreement to effect a change in the interest rate on the applicable portion of the Loan then outstanding, with respect to which such Interest Rate Election was made, such change to occur on the Interest Adjustment Date next succeeding receipt of such telecopied or telephonic Interest Rate Election by the Lender. Any telecopied or telephonic Interest Rate Election received by the Lender after 1:00 P.M. on a Business Day shall be deemed, for all purposes of this Note to have been received prior to 1:00 P.M. on the next succeeding Business Day.

"Loan" or "Loans" means the indebtedness outstanding under this Note, and where the context so requires, as in the definition of Prime Rate Loan, all or a portion of such indebtedness.

"Loan Agreement" means the Loan Agreement between Borrower and Lender of even date.

"Prime Rate Loan" means a Loan bearing interest at the Floating Rate (as defined in the Note).

2. VOLUNTARY AND MANDATORY PREPAYMENTS AND PAYMENTS.

(A) VOLUNTARY PREPAYMENTS AND PAYMENTS. All or any portion of the unpaid principal balance of any Prime Rate Loan may be prepaid at any time by a payment to the Lender of immediately available Dollars by the Borrower and all or any portion of the unpaid principal balance of any Fixed Rate Loan may be prepaid or paid to the Lender by a payment of immediately available Dollars on the Interest Adjustment Date for such Loan, upon concurrent telephonic or telecopied notice promptly confirmed in writing, without premium or penalty, except as provided in paragraph 4 hereof; provided that all such payments and prepayments of Fixed Rate Loans shall be accompanied by the interest accrued on the principal amount being paid or prepaid through the date of payment or prepayment and provided further that each such partial payment or prepayment of principal of a Fixed Rate Loan shall be in such amount so that each outstanding Fixed Rate Loan remains in a principal amount of at least One Hundred Thousand Dollars ($100,000) and, to the extent in excess thereof, in the amount of Fifty Thousand Dollars ($50,000) or an integral multiple thereof, and provided further that each such partial payment or prepayment of principal of a Prime Rate Loan shall be in the amount of at least One Hundred Thousand Dollars ($100,000) and, to the extent in excess thereof, in the amount of Fifty Thousand Dollars ($50,000) or an integral multiple thereof. The Borrower's notice of payment or prepayment to the Lender shall designate whether such payment or prepayment is a payment or prepayment of one or more Prime Rate Loans or Fixed Rate Loans.

(B) MANDATORY PAYMENTS. If at any time the aggregate principal amount of the Loans shall exceed the maximum stated amount of this Note, the Borrower shall immediately pay to the Lender in immediately available Dollars the amount of such excess, such payment to be accompanied by Borrower's written notice designating whether such payment is a payment of one or more Prime Rate Loans or Fixed Rate Loans.

(C) ALLOCATION OF PAYMENT AND PREPAVMENTS. In the event that or to the extent that at the time of any payment or prepayment of all or any portion of the Loans, the Borrower fails to provide the Lender with telephonic or telecopied notice, the former confirmed in writing and/or written notice designating whether such payment or prepayment is a payment or prepayment of Prime Rate Loans or Fixed Rate Loans, the Lender shall allocate any such payment or prepayment to outstanding Prime Rate Loans, if any, until paid or prepaid in full and thereafter to outstanding Fixed Rate Loans. In the event that any mandatory payment is required under subparagraph 2(B) or upon acceleration or for any other reason, and on the date any such payment is due, the amount of Prime Rate Loans, if any, plus the amount of Fixed Rate Loans as to which such date is an Interest Adjustment Date for such Fixed Rate Loans is less than the amount of such required payment or prepayment, such payment or prepayment shall nevertheless be paid in full by the Borrower when due and the proceeds thereof will, to the extent not directed to be applied to specific Loans by Borrower's above-referenced designation, be applied first to outstanding Prime Rate Loans until paid in full and thereafter to the Fixed Rate Loans.

3. INTEREST IN ABSENCE OF INTEREST RATE ELECTION.

If at any time all or any portion of the outstanding principal balance of the Loans is not subject to an Interest Rate Election because an Interest Adjustment Date occurs and the Lender has not received a timely Interest Rate Election from the Borrower which is effective in accordance with the terms and conditions of this Revolving Note on such Interest Adjustment Date, the interest rate on all or said portion of said outstanding principal balance shall thereupon be and remain the Prime Rate until occurrence of an Interest Adjustment Date applicable to said principal balance of the Loans for which the Lender shall have received a timely Interest Rate Election effective in accordance with the terms and conditions of this

Revolving Note on such Interest Adjustment Date and which elects another available interest rate on all or said portion of said outstanding principal balance of the Loans.

4. SPECIAL COST OF FUNDS PROVISION.

The Fixed Rate Loans shall be subject to and governed by the following terms and conditions:

(A) INTEREST RATE ELECTIONS. The Borrower shall have the right, by submission of an Interest Rate Election to the Lender, to elect that the interest rate payable on all or any portion of the Prime Rate Loans, or on all or any portion of the Fixed Rate Loans on an Interest Adjustment Date applicable thereto, shall be the Fixed Rate, as the same shall exist on the date in question, for such term (the "Fixed Rate Term") of not less than thirty (30) days and not more than four (4) years as the Lender shall offer to the Borrower and the Borrower shall select. The Borrower shall have the right to make up to three (3) such elections at any one time provided that each election is with respect to at least One Hundred Thousand Dollars ($100,000) of principal and, to the extent in excess thereof, in the amount of Fifty Thousand Dollars ($50,000) or an integral multiple thereof. Once a Fixed Rate becomes applicable, such Fixed Rate must remain in effect for the applicable Fixed Rate Term. An Interest Rate Election electing the Fixed Rate shall only apply to that portion of the Loans outstanding at the time of election and specified in such Interest Rate Election. Once a Fixed Rate becomes applicable pursuant to the third (3rd) Interest Rate Election, unless the Lender shall otherwise agree in writing, the applicable Interest Rate payable under the Loans on all subsequent Advances of the Loans shall be at the Prime Rate until the expiration of one of the then applicable Fixed Rate Terms, at which time the Borrower may again elect a Fixed Rate in accordance with the terms of this paragraph 4, it being understood that at no time shall the Lender be under any obligation to permit the Borrower to have more than three (3) Interest Rate Elections electing the Fixed Rate outstanding as to any portions of the Loan. On the last Business Day of any agreed upon Fixed Rate Term then in effect, the Borrower may submit to the Lender a new Interest Rate Election electing the Fixed Rate, at which time the Lender shall inform the Borrower of the Fixed Rate and the Fixed Rate Term which the Lender is then prepared to offer the Borrower, and the Borrower shall immediately elect whether or not to accept same. Upon the Borrower's making any telephonic election of a Fixed Rate, the Borrower shall contemporaneously submit to the Lender a written Interest Rate Election specifying that commencing with the date in question, the applicable interest rate for a specified portion of the Loans shall be specified Fixed Rate which shall remain in effect for a specified Fixed Rate Term.

(B) VOLUNTARY PREPAYMENT. The Borrower shall be permitted to voluntarily prepay, in whole or in part, any Fixed Rate Loan at any time, subject to the Borrower giving the Lender not less than five (5) Business Days prior written notice thereof, subject to current market conditions, as determined by the Lender, and, subject to the Borrower's payment to the Lender of a prepayment premium in an amount computed pursuant subparagraph 4(D) below. In the event of any such voluntary prepayment the date upon which such computation of such prepayment premium shall be based (the "Determination Date") shall be the date upon which such prepayment is made.

(C) INVOLUNTARY PREPAYMENT. If the obligations of the Borrower to the Lender evidenced by this Note shall be accelerated, then upon the Lender's demand made at any time thereafter the Borrower shall pay to the Lender a prepayment premium in an amount computed pursuant to subparagraph (D) below. In such event the Determination Date upon which the computation of such prepayment premium shall be based shall be such date as may be selected by the Lender, in its sole discretion, within the period commencing with the date of such acceleration and ending on the last day of any applicable Fixed Rate Term. In the event of such acceleration, an involuntary prepayment of all Fixed Rate Loans shall be deemed to have occurred upon the Determination Date selected by the Lender regardless of whether funds are actually received by the Lender.

(D) PREPAYMENT PREMIUM. The prepayment premium to be paid by the Borrower shall be computed as follows: the latest published rate preceding the Determination Date for United States Treasury Notes or Bills (Bills on a discounted basis shall be converted to a bond equivalent) as published weekly in the Federal Reserve Statistical Release with a maturity date closest to the expiration date of the applicable Fixed Rate Term shall be subtracted from the applicable Fixed Rate. If the result is zero or a negative number, there shall be no prepayment premium. If the result is a positive number, then the resulting percentage shall be multiplied by the amount of the principal balance being prepaid. The resulting amount will be divided by three hundred sixty (360) and multiplied by the number of days remaining between the Determination Date and the expiration date of the applicable Fixed Rate Term (the "Unexpired Term"). Said amount shall be reduced to present value calculated by using the above referenced United States Treasury Note or Bill rate and assuming that said amount will be paid in equal monthly installments over the Unexpired Term and assuming further that the first such monthly installment will be paid thirty (30) days after the Determination Date. The resulting amount shall be the prepayment premium due to the Lender upon notice by the Lender to the Borrower of the amount thereof and shall thereupon be paid by the Borrower to the Lender in immediately available Dollars.

(E) MULTIPLE FIX RATE TERMS. In the event that more than one Fixed Rate and/or Fixed Rate Term in applicable to the Loans, then separate computations shall be made of the prepayment premium applicable to each Fixed Rate and fixed Rate Term and the prepayment premium payable by the Borrower to the Lender shall be the sum of the amounts so determined. A certificate of an authorized officer of the Lender as to the amount of such costs shall be conclusive and binding on the Borrower and the Lender, absent manifest error.

AMENDMENT TO LOAN AGREEMENT AND PROMISSORY NOTE

This Amendment to Loan Agreement and Promissory Note dated as of May 15, 1997 is entered into by and between CytoTherapeutics, Inc., a Delaware corporation ("Borrower") and Fleet National Bank, a national banking association organized and existing under the laws of the United States of America ("Lender").

WHEREAS, Borrower and Lender entered into a Loan Agreement as of May 15, 1996 (the "Loan Agreement"); and

WHEREAS, the obligations of Borrower to Lender in connection with the Loan Agreement are evidenced by a Promissory Note of Borrower in favor of Lender in the maximum principal amount of Two Million ($2,000,000) Dollars (the "Note"); and

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

NOW THEREFORE, in consideration of the mutual covenants and agreements hereinafter set forth and for the other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties agree as follows:

1. Paragraph 1.10 of the Loan Agreement is amended in its entirety to read as follows: "1.10 Conversion Date means May 17, 1998."

2. The first sentence of the fourth paragraph of the Note is hereby amended in its entirety to read as follows:

"The outstanding principal balance hereunder on May 17, 1998 shall be paid in eight (8) equal consecutive quarterly installments of principal together with interest thereon commencing August 1, 1998 and continuing on the same day of each November, February, May and August thereafter with a final payment of the entire balance then remaining due under this Note on May 1, 2000."

3. Borrower represents and warrants to Lender that there exists no Event of Default as defined in the Loan Agreement and that all representations and warranties of Borrower set forth therein remain true, complete and correct as of the date hereof.

4. Except as specifically amended hereby, all terms and provisions of the Loan Agreement, the Note and the Security Documents (as defined in the Loan Agreement) remain in full force and effect.

Dated and effective as of the 15th day of May, 1997.

WITNESS: CytoTherapeutics, Inc.

By: _____

Title: _____

WITNESS: Fleet National Bank

By: _____

Title: _____

SUBSIDIARIES OF CYTOTHERAPEUTICS, INC.

NAME	JURISDICTION OF INCORPORATION
StemCells, Inc.	California

EXHIBIT 23.1

Consent of Independent Auditors

We consent to the incorporation by reference in the Registration Statement (Form S-8 No. 33-49524 and 333-29335) pertaining to the 1988 Incentive Stock Plan, 1992 Equity Incentive Plan, 1992 Employee Stock Purchase Plan and 1992 Stock Option Plan for Non-Employee Directors, in the Registration Statement (Form S-8 No. 333-10773) pertaining to the 1992 Equity Incentive Plan, in the Registration Statement (Form S-8 No. 333-37313) pertaining to the 1996 StemCells, Inc. Stock Option Plan and the 1997 CytoTherapeutics, Inc. StemCells Research Stock Option Plan and in the Registration Statements (Form S-3 No. 33-68900 and No. 333-91228) of CytoTherapeutics, Inc. and in the related Prospectuses of our report dated February 6, 1998, with respect to the consolidated financial statements and schedule included in the Annual Report (Form 10-K) of CytoTherapeutics, Inc. for the year ended December 31, 1997.

ERNST & YOUNG LLP

Boston, Massachusetts
March 25, 1998

YEAR	
	DEC-31-1997
	DEC-31-1997
	15,941,701
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	0
	0
	0
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	0
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	44,301,466
	0
	10,617,443
	0
	0
	33,105,617
	0
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	0
	(18,113,580)
	0
	0
	0
	(18,113,580)
	(1.08)
	(1.08)

CAUTIONARY FACTORS RELEVANT TO FORWARD-LOOKING INFORMATION

CYTOTHERAPEUTICS, INC. (THE "COMPANY") WISHES TO CAUTION READERS THAT THE FOLLOWING IMPORTANT FACTORS, AMONG OTHERS, IN SOME CASES HAVE AFFECTED AND IN THE FUTURE COULD AFFECT THE COMPANY'S RESULTS AND COULD CAUSE ACTUAL RESULTS AND NEEDS OF THE COMPANY TO VARY MATERIALLY FROM FORWARD-LOOKING STATEMENTS MADE IN THIS ANNUAL REPORT BY THE COMPANY ON THE BASIS OF MANAGEMENT'S CURRENT EXPECTATIONS. THE BUSINESS IN WHICH THE COMPANY IS ENGAGED IS RAPIDLY CHANGING, EXTREMELY COMPETITIVE AND INVOLVES A HIGH DEGREE OF RISK, AND ACCURACY WITH RESPECT TO FORWARD-LOOKING PROJECTIONS IS DIFFICULT.

EARLY STAGE DEVELOPMENT; HISTORY OF OPERATING LOSSES -- Substantially all of the Company's revenues to date have been derived, and for the foreseeable future substantially all of the Company's revenues will be derived, from collaborative agreements, research grants and income earned on invested funds. The Company will incur substantial operating losses in the future as the Company conducts its research, development, clinical trial and manufacturing activities. There can be no assurance that the Company will achieve revenues from product sales or become profitable.

FUTURE CAPITAL NEEDS; UNCERTAINTY OF ADDITIONAL FUNDING -- The development of the Company's products will require the commitment of substantial resources to conduct the time-consuming research, preclinical development and clinical trials that are necessary for regulatory approvals and to establish production and marketing capabilities, if such approvals are obtained. The Company will need to raise substantial additional funds to continue its product development efforts and intends to seek such additional funds through partnership, collaborative or other arrangements with corporate sponsors, public or private equity or debt financings, or from other sources. Future cash requirements may vary from projections based on changes in the Company's research and development programs, progress in preclinical and clinical testing, the Company's ability to enter into, and perform successfully under, collaborative agreements, competitive and technological advances, the need to obtain proprietary rights owned by third parties, facilities requirements, changes in regulations and other factors. Lack of necessary funds may require the Company to delay, reduce or eliminate some or all of its research and product development programs or to license its potential products or technologies to third parties. No assurance can be given that funding will be available when needed, if at all, or on terms acceptable to the Company.

UNCERTAINTIES OF CLINICAL DEVELOPMENT AND NEW MODE OF THERAPY -- None of the Company's proposed products has been approved for commercial sale or entered Phase III clinical trials. Even if the Company's proposed products appear to be promising at an early stage of research or development such products may later prove to be ineffective, have adverse side effects, fail to receive necessary regulatory approvals, be difficult or uneconomical to manufacture or market on a commercial scale, be adversely affected by government price controls or limitations on reimbursement, be precluded from commercialization by proprietary rights of third parties, by regulatory restrictions, or be subject to significant competition from other products. There can be no assurance that the Company will be able to demonstrate, as required, that its implants, on a consistent basis and on a commercial scale, among other things: (i) successfully isolate transplanted cells from the recipient's immune system; (ii) remain biocompatible with the tissue into which they are implanted, including, for certain implants, brain tissue; (iii) adequately maintain the viability of cells contained within the membrane for a sufficiently long time to be efficacious and commercially viable; (iv) safely permit the therapeutic substances produced by the cells within the membrane to pass through the membrane unto the patient in controlled doses for extended periods; and (v) are sufficiently durable for the intended indication. While clinicians have generally had little difficulty in retrieving the Company's implants, there have been cases where the implant broke on attempted explant. The Company has changed its implantation procedure and its implants and is continuing a program of developing stronger implants. In addition, the viability of implanted encapsulated cells varies depending of the cell type, the implantation location and other factors. Lack of viability could restrict certain of the Company's programs to indications

where long-term delivery of the therapeutics substances is not required. There can also be no assurance that the products that may be generated in the Company's stem cell programs will: (i) survive and persist in the desired locations, (ii) provide the therapeutic benefits intended, (iii) properly differentiate and integrate into existing tissue in the desired manner, or (iv) not cause tumors or other side effects.

There has been increasing regulatory concern about the risks of cell transplantation. Concern has focused on the use of cells derived from cows (such as are used in the Company's pain program) and cells from primates and pigs. The United Kingdom has adopted a moratorium on xenotransplantation pending further research and discussion; the EC Commission has introduced a ban on the use of "high-risk material" from cattle and sheep in the Member States of the European Union in the manufacture of pharmaceuticals (this ban would apparently not include the type of cells used in the Company's pain program). In addition, the FDA has proposed guidelines which impose significant constraints on the conduct of clinical trials utilizing xenotransplantion and are likely to significantly affect the cost of producing the Company's products using nonhuman cells; such costs could make the Company's products cost more to produce than the Company receives for their production. Furthermore, the FDA has published a "Proposed Approach to Regulation of Cellular and Tissue-Based Products" which relates to the use of human cells. The Company cannot presently determine the effects of such actions nor what other actions might be taken. Restrictions on the testing or use of cells, whether human or nonhuman, as human therapeutics, could adversely affect the Company's product development programs and the Company itself. See "Government Regulation."

DEPENDENCE ON OUTSIDE PARTIES -- The Company's strategy for the research, development, commercialization and marketing of its products contemplates that the Company will enter into various arrangements with corporate sponsors, pharmaceutical companies, universities, research groups and others. There is no assurance that the Company will be able to enter into any additional arrangements on terms acceptable to the Company, or successfully perform its obligations under its existing or any additional arrangements. If any of the Company's collaborators fails to perform its obligations in a timely manner or terminate their agreement with the Company, the development or commercialization of the Company's product candidate or research program under such collaborative agreement may be adversely affected. Moreover, the Company is particularly dependent on its pain program partner, Astra AB, because changes in the development of this particular program may significantly affect the Company's stock price. In addition, because of the Company's obligation to repurchase certain of the stock it sold to Genentech in connection with certain terminations of the Parkinson's Agreement, any such termination could have an adverse effect on the Company's liquidity.

NEED FOR AND UNCERTAINTY OF OBTAINING PATENT PROTECTION -- Patent protection for products such as those the Company proposes to develop is highly uncertain and involves complex factual and evolving legal questions. No assurance can be given that any patents issued or licensed to the Company will not be challenged, invalidated or circumvented, or that the rights granted under such patents will provide competitive advantages to the Company.

EXISTENCE OF THIRD PARTY PATENTS AND PROPRIETARY RIGHTS; NEED TO OBTAIN LICENSE -- A number of pharmaceutical, biotechnology and other companies, universities and research institutions have filed patent applications or have been issued patents relating to cell therapy and encapsulation and other technologies potentially relevant to or required by the Company's expected products. The Company cannot predict which, if any, of such applications will issue as patents or the claims which might be allowed. The Company is aware that a number of entities have filed applications relating to stem and/or progenitor cells. The Company is also aware of a number of third-party patent applications and patents relating to cell encapsulation or claiming use of genetically modified cells to treat disease, disorder or injury. In particular, the Company is aware of a third-party U.S. patent which relates the use of cells for alleviating chronic pain in humans and of two issued U. S. patents claiming certain methods for treating defective, diseased or damaged cells in the mammalian CNS by grafting genetically modified cells. The Company cannot predict

the effect of existing patent applications and patents on future unencapsulated products. In addition, the Company is aware of third-party patents and patent applications claiming rights to the neurotrophic factors (such as CNTF, NT 4/5, Neurturin, and CT-1) which the Company hopes to deliver with its technology, and to the production of these factors through the use of genetically modified cells. The Company expects to use genetically modified cells to produce these factors for use in its encapsulated products and expects that it may wish to genetically modify its stem/progenitor cells. The Company may also be required to seek licenses in regard to other cell lines, the techniques used in creating, obtaining or maintaining such cell lines, the materials used in the manufacture of its implants or otherwise. There can be no assurance that the Company will be able to establish collaborative arrangements or obtain licenses to the foregoing technology or to other necessary or desirable technology on acceptable terms, if at all, or that the patents underlying any such licenses will be valid and enforceable. See "Patents, Proprietary Rights and Licenses" in the Company's Annual Report on Form 10-K.

GOVERNMENT REGULATION -- The Company's research, preclinical development and clinical trials, as well as the manufacturing and marketing of its potential products, are subject to extensive regulation by governmental authorities in the United States and other countries. The process of obtaining FDA and other required regulatory approvals is lengthy, expensive and uncertain. There can be no assurance that the Company or its collaborators will be able to obtain the necessary approvals to commence or continue clinical testing or to manufacture or market its potential products in anticipated time frames, if at all. In addition, several legislative proposals have been made to reform the FDA. If such proposals are enacted they may result in significant changes in the regulatory environment the Company faces. These changes could result in different, more costly or more time consuming approval requirements for the Company's products, in the dilution of FDA resources available to review the Company's products, or in other unpredictable consequences. See "Government Regulation" in the Company's Annual Report on Form 10-K.

SOURCES OF CELLS AND OTHER MATERIALS -- The Company's potential products require genetically engineered cell lines or living cells harvested from animal or human sources. There can be no assurance that the Company will successfully identify or develop sources of the cells required for its potential products and obtain such cells in quantities sufficient to satisfy the commercial requirements of its potential products. These supply limitations may apply, in particular, to primary cells which must be drawn directly from animal or human sources, such as the bovine adrenal chromaffin cells currently used in the Company's product for the treatment of pain. As an alternative to primary cells, the Company is developing products based on the use of genetically altered cells. Intellectual property rights to important genetic constructs used in developing such cells, including the constructs used to develop cells producing neurotrophic factors, are or may be claimed by one or more companies, which could prevent the Company from using such cells. In addition, many suppliers of materials used by the Company in its media, implants, and other components have restricted the use of such materials for implantation into humans; if the Company cannot obtain the necessary materials for its implants, the Company would be adversely affected.

MANUFACTURING UNCERTAINTIES -- The Company's pilot manufacturing plant, may not have sufficient capacity to permit the Company to produce all the products for all of the clinical trials it anticipates developing. In addition, the Company has not developed the capability to commercially manufacture any of its proposed products and is unaware of any other company which has manufactured any membrane-encapsulated cell product on a commercial scale. There can be no assurance that the Company will be able to develop the capability of manufacturing any of its proposed products at a cost or in the quantities necessary to make a commercially viable product, if at all.

COMPETITION -- Competitors of the Company are numerous and include major pharmaceutical and chemical companies, biotechnology companies, universities and other research institutions. Currently, several of these competitors market and sell therapeutic products for the treatment of chronic pain, Parkinson's disease and other CNS conditions. In addition, most of the Company's competitors have

substantially greater capital resources, experience in obtaining regulatory approvals and, in the case of commercial entities, experience in manufacturing and marketing pharmaceutical products, than the Company. A number of other companies are attempting to develop methods of delivering therapeutic substances within or across the blood brain barrier. There can be no assurance that the Company's competitors will not succeed in developing technologies and products that are more effective than those being developed by the Company or that would render the Company's technology and products obsolete or non-competitive. See "Competition" in the Company's Annual Report on Form 10-K.

DEPENDENCE ON KEY PERSONNEL -- The Company is highly dependent on the principal members of its management and scientific staff and certain of its outside consultants. Loss of the services of any of these individuals could have a material adverse effect on the Company's operations. In addition, the Company's operations are dependent upon its ability to attract and retain additional qualified scientific and management personnel. There can be no assurance the Company will be able to attract and retain such personnel on acceptable terms given the competition among pharmaceutical, biotechnology and health care companies, universities and research institutions for experienced personnel.

REIMBURSEMENT AND HEALTH CARE REFORM -- In both domestic and foreign markets, sales of the Company's potential products will depend in part upon the availability and amounts of reimbursement from third-party health care payor organizations, including government agencies, private health care insurers and other health care payors such as health maintenance organizations and self-insured employee plans. There is considerable pressure to reduce the cost of therapeutic products. There can be no assurance that reimbursement will be provided by such payors at all or without substantial delay, or, if such reimbursement is provided, that the approved reimbursement amounts will provide sufficient funds to enable the Company to sell its products on a profitable basis. See "Reimbursement and Health Cost Control" in the Company's Annual Report on Form 10-K.