

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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2000

Commission File Number 0-9314

ACCESS PHARMACEUTICALS, INC.

-----  
(Exact name of registrant as specified in its charter)

Delaware

83-0221517

-----  
(State of Incorporation)

-----  
(I.R.S. Employer I.D. No.)

2600 Stemmons Frwy, Suite 176, Dallas, TX 75207

-----  
(Address of principal executive offices)

Telephone Number (214) 905-5100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirement for the past 90 days.

Yes  No  
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The number of shares outstanding of each of the issuer's classes of common stock, as of November 14, 2000, was 12,783,225 shares of Common Stock, \$0.01 par value per share.

Total No. of Pages 14

PART I -- FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

The response to this Item is submitted as a separate section of this report.

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS

OVERVIEW

Access Pharmaceuticals, Inc. is a Delaware corporation in the development stage. We are an emerging pharmaceutical company focused on developing both novel low development risk product candidates and technologies with longer-term major product opportunities. Together with our subsidiaries, we have proprietary patents or rights to five technology platforms: synthetic polymers, bioerodible hydrogels, ResiDerm TM, carbohydrate targeting technology and agents for the prevention and treatment of viral disease, including HIV. In addition, Access' partner Block Drug Company, or Block, is marketing in the United States Aphthasol TM, the first FDA approved product for the treatment of canker sores. We are developing new formulations and

delivery forms to evaluate this product in additional clinical indications. We have licensed the rights to amlexanox for the treatment of canker sores, oral diseases and topical applications from Block for certain countries excluding the U. S. and the worldwide rights for certain additional indications including mucositis.

Except for the historical information contained herein, the following discussions and certain statements in this Form 10-Q are forward-looking statements that involve risks and uncertainties. In addition to the risks and uncertainties set forth in this Form 10-Q, other factors could cause actual results to differ materially, including but not limited to our research and development focus, uncertainties associated with research and development activities, uncertainty associated with, and the results of, preclinical and clinical testing, future capital requirements, anticipated option and licensing revenues, dependence on others, ability to raise capital, and other risks detailed in our reports filed under the Securities Exchange Act, including but not limited to our Annual Report on Form 10-K for the year ended December 31, 1999.

Since our inception, we have devoted our resources primarily to fund our research and development programs. We have been unprofitable since inception and to date have received limited revenues from the sale of products. No assurance can be given that we will be able to generate sufficient product revenues to attain profitability on a sustained basis or at all. We expect to incur losses for the next several years as we continue to invest in product research and development, preclinical studies, clinical trials and regulatory compliance. As of September 30, 2000, our accumulated deficit was \$30,289,000 of which \$8,894,000 was the result of the write-off of excess purchase price.

#### RECENT DEVELOPMENTS

On September 20, 2000, we completed a \$13.5 million convertible note offering. The offering was placed with three investors. The note has a fixed conversion price of \$5.50 per share of common stock and is not convertible for at least twelve months. The note pays 7.0% per annum for the first twelve months and if not converted at that time the note will be adjusted to 7.7% per annum. The note is due September 13, 2005.

2

In addition, on September 13, 2000 we completed a transaction offering 250,000 shares of treasury stock to an individual at \$5.50 share. We received gross proceeds of \$1.4 million from this sale.

On August 25, 2000 we issued 142,857 shares of our common stock to Mipharm SpA in connection with an investment agreement between us and Mipharm that granted Mipharm the right to acquire shares at \$3.50 per share.

#### OTHER DEVELOPMENTS

On July 21, 2000, we initiated a voluntary odd-lot stock buy-back program through which stockholders who own 25 or fewer shares of our common stock, or Small-lot Stockholders, may elect to tender their shares for sale to Access. Under this program, we will repurchase the shares held by Small-lot Stockholders who validly tender their shares pursuant to the terms of the odd-lot stock buy-back program. The per share purchase price to be paid by Access to each participating Small-lot Stockholder for each share validly tendered by such Small-lot Stockholder pursuant to the terms of the odd-lot stock buy-back program will be the closing price of our common stock, as quoted on the American Stock Exchange, on the date that a completed package, addressed to Access and containing the Small-lot Stockholder's original stock certificate(s) and a signed and properly completed Letter of Transmittal, is post dated. This odd-lot stock buy-back program will remain available to Small-lot Stockholders until November 30, 2000 unless extended.

On June 26, 2000 the Food and Drug Administration (FDA) cleared our Investigational New Drug Application (IND) to commence Phase III clinical development in the United States for OraDisc TM for the treatment of canker sores. OraDisc TM, a polymer disc formulation which adheres to the disease site and slowly erodes, locally releasing the drug, is potentially an improved delivery vehicle for the oral delivery of amlexanox. Utilizing this technology, it is anticipated that higher drug concentrations will be achieved at the disease site, increasing the effectiveness of the product.

Previously, in April 2000, the FDA cleared our IND to commence a clinical trial program for OraDisc TM and the initial irritation study conducted under the IND has been successfully completed. The Phase III trial is being conducted at 15 centers in the United States and one site in Europe. The clinical trial will be a double-blind placebo controlled study with a no treatment arm which will evaluate the ability of OraDisc TM to accelerate healing and reduce pain once a canker sore has developed. This study has a similar design to the studies conducted with the 5% amlexanox oral paste where the product was proven effective accelerating healing and reducing pain. Currently, a Phase III clinical study is being conducted in Northern Ireland to evaluate OraDisc TM for the prevention of canker sores by applying the product at the first sign or symptom of the disease.

Two European clinical studies of Zindaclin TM, which incorporates clindamycin in the ResiDerm TM delivery system for the treatment of acne, have been completed. These studies are a pharmacokinetics study to determine the systemic absorption of Zindaclin TM and a pivotal Phase III study evaluating the efficacy of the product. The results of these studies are expected to be available soon. The ResiDerm TM delivery system uses zinc ions to enhance the penetration of topically applied drugs into the skin and the accumulation of drug in the skin, offering the prospect of improved clinical effectiveness and reduced systemic side effects.

OraRinse TM is an adhesive oral liquid formulation of amlexanox for the treatment of mucositis, a severe side effect of chemotherapy and radiation treatment of cancer patients. The Phase II study to evaluate the potential of OraRinse TM to prevent or reduce the severity of mucositis in head and neck cancer patients undergoing radiation with or without chemotherapy is approximately 50% enrolled. The study is expected to be completed in the 1st quarter 2001.

3

Polymer Platinate, AP5280, is a chemotherapeutic agent incorporating platinum bound to a polymer designed to improve the clinical benefit of platinum therapy in cancer patients by concentrating the drug in the tumor and reducing the side effects. A Phase I study to determine the dosing levels of the product, was recently initiated and three patients have already received treatment. The study is expected to take approximately 9-12 months depending on the number of patients required to determine maximum dosing levels.

During the second quarter we completed two self-managed private placement sales of our common stock, pursuant to which we sold 250,000 and 507,750 shares of our common stock at per share prices of \$3.00 and \$5.00, respectively. We received gross proceeds of \$3.3 million from these sales. In addition, on March 1, 2000, with the assistance of an investment bank, we completed the closing of a separate private placement offering of 4.8 million shares of common stock, at a per share price of \$2.50, for which we received gross proceeds of \$12.0 million. In accordance with the offering terms of this \$12.0 million private placement, the placement agent for the offering received warrants to purchase 382,315 shares of our common stock at \$2.50 per share, and elected to receive 520,905 shares of common stock in lieu of certain sales commissions. The funds from the private placements will be used principally for general corporate purposes to support our operations and to fund clinical development of our portfolio of product candidates. Exclusive of any payments received from strategic partners, we have funds to support operations for approximately 48 months. We registered the shares issued in each of the private placements on a Form S-3 registration statement that we initially filed with the Securities and Exchange Commission on May 25, 2000.

On March 28, 2000, our application for listing on the American Stock Exchange, or AMEX, was approved and we began trading on AMEX on March 30, 2000 under the symbol AKC.

On February 25, 2000 we signed licensing agreements with Mipharm S.p.A. Pursuant to these agreements, we granted to Mipharm marketing and manufacturing rights for amlexanox for numerous indications including the prevention and treatment of canker sores and mucositis, oral lichen planus and atopic dermatitis. We also granted manufacturing rights for Europe to Mipharm for the products covered by the agreements. These licensing agreements cover Italy, Switzerland, Turkey and Lebanon and relate to:

\* the 5% paste formulation, approved in the United States for the treatment

of canker sores, which is in the regulatory process in Europe;

- \* the OraDisc TM formulation which is in Phase III clinical development for the prevention and treatment of canker sores;
- \* OraRinse TM which has commenced Phase II clinical evaluation for the prevention and treatment of mucositis;
- \* the 5% amlexanox cream formulation for the treatment for atopic dermatitis; and
- \* a 5% amlexanox gel for the treatment of oral lichen planus.

Mipharm also has the option to license other Access product developments in the fields of Dermatology and Gynecology in the territory covered by the license agreements. In addition, under the terms of the agreements, Mipharm paid up-front licensing fees and will make milestone payments and Access will receive a percentage of the product sales made in the territory. Moreover, pursuant to an investment agreement with Mipharm, Mipharm made an equity investment in Access in 2000 and has the right to make an additional equity investments in Access up to the first quarter in 2002.

4

## LIQUIDITY AND CAPITAL RESOURCES

As of September 30, 2000, our principal source of liquidity was \$26,845,000 of cash and cash equivalents, short term investments and certificates of deposits. Working capital as of September 30, 2000 was \$25,718,000, representing an increase in working capital of \$25,630,000 as compared to the working capital as of December 31, 1999 of \$88,000. The increase in working capital was due to the funds received from our March, May and September 2000 private placements, our September 2000 issuance of convertible notes and licensing revenues.

Since inception, our expenses have significantly exceeded revenues, resulting in an accumulated deficit as of September 30, 2000 of \$30,289,000. We have funded our operations primarily through private sales of common stock and convertible notes. Contract research payments, licensing fees and milestone payments from corporate alliances and mergers have also provided funding for operations.

We have incurred negative cash flows from operations since inception, and have expended, and expect to continue to expend in the future, substantial funds to complete our planned product development efforts. We expect that our existing capital resources will be adequate to fund our current level of operations through the year 2004.

We will expend substantial funds to conduct research and development programs, preclinical studies and clinical trials of potential products, including research and development with respect to our newly acquired and developed technology. Our future capital requirements and adequacy of available funds will depend on many factors, including:

- \* the successful commercialization of amlexanox;
- \* the ability to establish and maintain collaborative arrangements with corporate partners for the research, development and commercialization of products;
- \* continued scientific progress in our research and development programs;
- \* the magnitude, scope and results of preclinical testing and clinical trials;
- \* the costs involved in filing, prosecuting and enforcing patent claims;
- \* competing technological developments;
- \* the cost of manufacturing and scale-up;
- \* the ability to establish and maintain effective commercialization arrangements and activities; and

- \* successful regulatory filings.

Third Quarter 2000 Compared to Third Quarter 1999.

Total research spending for the third quarter of 2000 was \$1,051,000, as compared to \$349,000 for the same period in 1999, an increase of \$702,000. The increase in expenses was the result of:

- \* higher clinical development and product development costs for the amlexanox projects: OraDisc TM (\$286,000), OraRinse TM (\$191,000) and amlexanox cream (\$14,000);
- \* higher external development costs for our polymer platinate project (\$147,000); and
- \* higher employee expenses due to additional scientific staff (\$64,000).

5

We expect that research spending will increase and remain higher than prior years' quarters as we intend to hire additional scientific and clinical staff, commence additional clinical trials and accelerate preclinical development activities as we continue to develop our product candidates.

Total general and administrative expenses were \$332,000 for the third quarter of 2000 as compared to \$293,000 for the same period in 1999, an increase of \$39,000. The change in spending for the periods was due primarily to the following:

- \* higher legal and accounting expenses (\$34,000);
- \* higher insurance costs due to clinical trial insurance (\$23,000); and
- \* other net increases (\$25,000).

Those increases were partially offset by lower patent costs (\$43,000).

Depreciation and amortization was \$110,000 for the third quarter 2000 as compared to \$84,000 for the same period in 1999, reflecting an increase of \$26,000. The increase in amortization is due to:

- \* amortization of goodwill of \$21,000 recorded as a result of the purchase of Virologix Corporation;
- \* amortization of licenses totaling \$13,000; offset by,
- \* lower depreciation (\$8,000) reflecting that some of our major assets have been fully depreciated.

Interest and miscellaneous income was \$236,000 for the third quarter of 2000 as compared to \$18,000 for the same period in 1999, an increase of \$218,000. The increase in interest income was due to higher cash and short-term investment balances in 2000 resulting from our private placements of common stock and our convertible note offering in 2000.

Interest expense was \$53,000 for the third quarter of 2000 as compared to \$3,000 for the same period in 1999, an increase of \$50,000. The increase in interest expense is due to interest accrued on the \$13.5 million convertible notes issued in September 2000 and amortization of debt issuance costs.

Net loss in the third quarter of 2000 was \$1,310,000, or a \$0.11 basic and diluted loss per common share, compared with a loss of \$711,000, or a \$0.13 basic and diluted loss per common share, for the same period in 1999.

Nine Months ended September 30, 2000 Compared to Nine Months ended September 30, 1999.

Total research spending for the nine months ended September 30, 2000 was \$2,723,000, as compared to \$1,042,000 for the same period in 1999, an increase of \$1,681,000. The increase in expenses was the result of:

- \* higher clinical development and product development costs for the amlexanox

projects: OraDisc TM (\$591,000), OraRinse TM (\$529,000) and amlexanox cream (\$63,000);

- \* higher external development costs for our polymer platinate project (\$304,000);
- \* higher employee expenses due to additional scientific staff (\$117,000);
- \* moving expenses for scientific personal (\$50,000); and
- \* recruitment expenses (\$27,000).

6

We expect research spending to increase and remain higher than prior years' quarters as we intend to hire additional scientific and clinical staff, commence additional clinical trials and accelerate preclinical development activities as we continue to develop our product candidates.

Total general and administrative expenses were \$1,205,000 for the nine months ended September 30, 2000 and 1999. Expenses increased in 2000 due to:

- \* higher salary and bonus expenses (\$138,000);
- \* higher listing fees due to our listing on the American Stock Exchange (\$30,000); and
- \* higher legal and accounting expenses (\$92,000).

These increases were offset by a reduction in warrant costs (\$260,000) due to warrants granted to consultants.

Depreciation and amortization was \$333,000 for the nine months ended September 30, 2000 as compared to \$177,000 for the same period in 1999, an increase of \$156,000. The increase in amortization is due to:

- \* amortization of goodwill of \$144,000 recorded as a result of the purchase of Virologix Corporation; and
- \* amortization of licenses totaling \$40,000.

These increases were offset by lower depreciation (\$28,000) reflecting that some of our major assets have been fully depreciated.

Interest and miscellaneous income was \$524,000 for the nine months ended September 30, 2000 as compared to \$37,000 for the same period in 1999, an increase of \$487,000. The increase in interest income was due to higher cash balances in 2000 resulting from our private placements of common stock and our convertible note offering in 2000.

Interest expense was \$56,000 for the nine months ended September 30, 2000 as compared to \$11,000 for the same period in 1999, an increase of \$45,000. The increase in interest expense is due to interest accrued on the \$13.5 million convertible notes issued in September 2000 and amortization of debt issuance costs.

Net loss for the nine months ended September 30, 2000 was \$3,836,000, or a \$0.37 basic and diluted loss per common share compared with a loss of \$2,398,000, or a \$0.58 basic and diluted loss per common share, for the same period in 1999.

## PART II -- OTHER INFORMATION

### ITEM 1 LEGAL PROCEEDINGS

The Company is not a party to any material legal proceedings.

### ITEM 2 CHANGES IN SECURITIES

On September 20, 2000, we completed a \$13.5 million convertible note offering. The offering

was placed with three investors each of whom, represented to us that they are accredited investors within the meaning of Rule 501 under the Securities Act of 1933, as amended. The note has a fixed conversion price of \$5.50 per share of common stock and is not convertible for at least twelve months. The note pays 7.0% per annum for the first twelve months and if not converted the note will be adjusted to 7.7% per annum. The note is due September 13, 2005. Total expenses of issuance were \$915,000. The shares associated with the convertible note offering have not been registered. The Company relied on Rule 506 and Section 4(2) of the 1933 Securities Act and the provisions of Regulation D as exemptions from the registration thereunder.

On September 13, 2000 we completed a transaction offering 250,000 shares of treasury stock at \$5.50 per share to an individual who represented to us that he is an accredited investor within the meaning of Rule 501 under the Securities Act of 1933, as amended. We received gross proceeds of \$1.4 million from this sale. The shares associated with this offering have not been registered. The Company relied on Rule 506 and Section 4(2) of the 1933 Securities Act and the provisions of Regulation D as exemptions from the registration thereunder.

On August 25, 2000 we issued 142,857 shares of our common stock to Mipharm SpA in connection with an investment agreement between us and Mipharm that granted Mipharm the right to acquire shares at \$3.50 per share. The Company relied on Regulation S and Section 4(2) of the Securities Act of 1933 as exemption from the registration thereunder.

The proceeds from the convertible note offering, the treasury stock sale and the Mipharm common stock sale will be used to fund the research and development, clinical development and general operations of the company.

#### ITEM 3 DEFAULTS UPON SENIOR SECURITIES

None

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

None

#### ITEM 5 OTHER INFORMATION

None

#### ITEM 6 EXHIBITS AND REPORTS ON FORM 8-K

Exhibits: 10.24 2000 Special Stock Option Plan and Agreement  
10.25 Form of Convertible Note  
27.1 Financial Data Schedule

Reports on Form 8-K:

None

#### SIGNATURES

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

ACCESS PHARMACEUTICALS, INC.

Date: November 14, 2000 By: /s/ Kerry P. Gray

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Kerry P. Gray  
President and Chief Executive Officer

Date: November 14, 2000 By: /s/ Stephen B. Thompson

-----  
Stephen B. Thompson

Access Pharmaceuticals, Inc. and Subsidiaries  
(a development stage company)

Condensed Consolidated Balance Sheets

<TABLE>

<CAPTION>

	September 30, 2000	December 31, 1999
	-----	
ASSETS	(unaudited)	
<S>	<C>	<C>
Current assets		
Cash and cash equivalents	\$ 7,166,000	\$ 869,000
Short term investments	7,864,000	-
Certificates of deposit	11,815,000	-
Accounts receivable	286,000	88,000
Accrued interest receivable	154,000	-
Prepaid expenses and other current assets	83,000	117,000
	-----	
Total current assets	27,368,000	1,074,000
Property and equipment, at cost	1,084,000	1,016,000
Less accumulated depreciation and amortization	(977,000)	(908,000)
	-----	
	107,000	108,000
Debt issuance costs	908,000	-
Licenses, net	921,000	899,000
Investments	150,000	150,000
Goodwill, net	2,176,000	2,361,000
Other assets	8,000	8,000
	-----	
Total assets	\$ 31,638,000	\$ 4,600,000
	=====	

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities

Accounts payable and accrued expenses	\$ 956,000	\$ 728,000
Accrued insurance premiums	36,000	77,000
Deferred revenues	658,000	155,000
Current portion of obligations under capital leases	-	26,000
	-----	

Total current liabilities 1,650,000 986,000

Convertible notes 13,500,000 -

Total liabilities 15,180,000 986,000

Commitments and contingencies - -

Stockholders' equity

Preferred stock - \$.01 par value; authorized 2,000,000 shares; none issued or outstanding	-	-
Common stock - \$.01 par value; authorized 50,000,000 shares; issued, 12,603,481 at September 30, 2000 and 6,089,763 at December 31, 1999	126,000	61,000
Additional paid-in capital	46,619,000	30,006,000
Treasury stock, 256 shares at September 30, 2000	2,000	-
Deficit accumulated during the development stage	(30,289,000)	(26,453,000)
	-----	



Total stockholders' equity	16,458,000	3,614,000
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Total liabilities and stockholders' equity	\$ 31,638,000	\$ 4,600,000
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</TABLE>

The accompanying notes are an integral part of these statements.

10

Access Pharmaceuticals, Inc. and Subsidiaries  
(a development stage company)

Condensed Consolidated Statements of Operations  
(unaudited)

<TABLE>

<CAPTION>

	Three Months ended September 30,		Nine Months ended September 30,		February 24, 1988
	2000	1999	2000	1999	(inception) to September 30, 2000
<S>	<C>	<C>	<C>	<C>	<C>
Revenues					
Research and development	\$ -	\$ -	\$ -	\$ -	\$ 2,711,000
Option income	-	-	-	-	2,164,000
Licensing revenues	-	-	-	-	325,000
Total revenues	-	-	-	-	5,200,000
Expenses					
Research and development	1,051,000	349,000	2,723,000	1,042,000	14,696,000
General and administrative	332,000	293,000	1,205,000	1,205,000	11,003,000
Depreciation and amortization	110,000	84,000	333,000	177,000	1,887,000
Write-off of excess purchase price	-	-	-	-	8,894,000
Total expenses	1,493,000	726,000	4,261,000	2,424,000	36,480,000
Loss from operations	(1,493,000)	(726,000)	(4,261,000)	(2,424,000)	(31,280,000)
Other income (expense)					
Interest and miscellaneous income	236,000	18,000	524,000	37,000	1,409,000
Interest and debt expense	(53,000)	(3,000)	(56,000)	(11,000)	(248,000)
	183,000	15,000	468,000	26,000	1,161,000
Loss before income taxes	(1,310,000)	(711,000)	(3,793,000)	(2,398,000)	(30,119,000)
Provision for income taxes	-	-	43,000	-	170,000
Net loss	\$(1,310,000)	\$(711,000)	\$(3,836,000)	\$(2,398,000)	\$(30,289,000)
Basic and diluted loss per common share	\$(0.11)	\$(0.13)	\$(0.37)	\$(0.58)	
Weighted average basic and diluted common shares outstanding	12,133,463	5,469,021	10,436,095	4,116,746	

</TABLE>

The accompanying notes are an integral part of these statements.

11

Access Pharmaceuticals, Inc. and Subsidiaries  
(a development stage company)

Condensed Consolidated Statements of Cash Flows  
(unaudited)

<TABLE>  
<CAPTION>

	February 24, Nine Months ended September 30, 1988		
	----- (inception) to September 30, 2000		
	2000	1999	September 30, 2000
	-----	-----	-----
<S>	<C>	<C>	<C>
Cash flows from operating activities:			
Net loss	\$(3,836,000)	\$(2,398,000)	\$(30,289,000)
Adjustments to reconcile net loss to cash used in operating activities:			
Write-off of excess purchase price	-	-	8,894,000
Warrants issued in payment of consulting expenses	-	296,000	865,000
Research expenses related to common stock granted	-	-	100,000
Depreciation and amortization	333,000	177,000	1,887,000
Deferred revenue	503,000	155,000	548,000
Licenses	(100,000)	(100,000)	(525,000)
Change in operating assets and liabilities:			
Accounts receivable	(198,000)	(3,000)	(287,000)
Accrued interest receivable	(154,000)	-	(154,000)
Prepaid expenses and other current assets	34,000	23,000	(84,000)
Other assets	-	-	(6,000)
Accounts payable and accrued expenses	187,000	(142,000)	230,000
Net cash used in operating activities	(3,231,000)	(1,992,000)	(18,821,000)
Cash flows from investing activities:			
Capital expenditures	(68,000)	(3,000)	(1,241,000)
Sales of capital equipment	-	-	15,000
Purchases of short term investments and certificates of deposit	(27,349,000)	-	(27,349,000)
Maturities of investments	7,673,000	-	7,673,000
Purchase of Virologix	-	(102,000)	(102,000)
Purchase of Tacora, net of cash acquired	-	-	(124,000)
Other investing activities	-	-	(150,000)
Net cash used in investing activities	(19,744,000)	(105,000)	(21,278,000)
Cash flows from financing activities:			
Proceeds from notes payable	-	-	721,000
Payments of principal on obligations under capital leases	(26,000)	(153,000)	(750,000)
Purchase of treasury stock	(752,000)	-	(752,000)
Cash acquired in merger with Chemex	-	-	1,587,000
Proceeds from convertible note, net	12,622,000	-	12,622,000
Proceeds from stock issuances, net	17,428,000	2,789,000	33,837,000
Net cash provided by financing activities	29,272,000	2,636,000	47,265,000
Net increase in cash and cash equivalents	6,297,000	539,000	7,166,000
Cash and cash equivalents at beginning of period	869,000	1,487,000	-
Cash and cash equivalents at end of period	\$ 7,166,000	\$ 2,026,000	\$ 7,166,000

</TABLE>

The accompanying notes are an integral part of these statements.

12

Access Pharmaceuticals, Inc. and Subsidiaries  
(a development stage company)

Notes to Condensed Consolidated Financial Statements  
Nine Months Ended September 30, 2000 and 1999  
(unaudited)

(1) Interim Financial Statements

The consolidated balance sheet as of September 30, 2000 and the consolidated statements of operations and cash flows for the three and nine months ended September 30, 2000 and 1999 were prepared by management without audit. In the opinion of management, all adjustments, including only normal recurring adjustments necessary for the fair presentation of the financial position, results of operations, and changes in financial position for such periods, have been made.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 1999. The results of operations for the periods ended September 30, 2000 are not necessarily indicative of the operating results which may be expected for a full year. The consolidated balance sheet as of December 31, 1999 contains financial information taken from the audited financial statements as of that date.

(2) Convertible Notes and Sales of Common Stock

On September 20, 2000, we completed a \$13.5 million convertible note offering. The offering was placed with three investors. The note has a fixed conversion price of \$5.50 per share of common stock and is not convertible for at least twelve months. The note pays 7.0% per annum for the first twelve months and if not converted at that time the note will be adjusted to 7.7% per annum. The note is due September 13, 2005. Total expenses of issuance were \$915,000.

On September 13, 2000 we completed a transaction offering 250,000 shares of treasury stock to an individual at \$5.50 share. We received gross proceeds of \$1.4 million from this sale.

On August 25, 2000 we issued 142,857 shares of our common stock to Mipharm SpA in connection with an investment agreement between us and Mipharm that granted Mipharm the right to acquire shares at \$3.50 per share.

(3) Short-term Investments

Short-term investments which consist of commercial paper and US government securities, are carried at cost.

13

EX-10.24  
ACCESS PHARMACEUTICALS, INC.  
2000 Special Stock Option Plan and Agreement

This 2000 Special Stock Option Plan and Agreement, is dated as of the 11th day of February, 2000 between Access Pharmaceuticals, Inc., a Delaware corporation (hereinafter called the "Company") and Kerry P. Gray called the "Grantee".

RECITALS:

A. On February 11, 2000 (the "Grant Date"), the Company adopted this 2000 Special Stock Option Plan and Agreement (the "Plan"). This Plan provides for the award of an option to purchase 500,000 shares of the authorized but unissued shares of the common stock, \$.01 par value per share, of the Company ("Common Stock") to the Grantee;

B. The Grantee has been designated by the Board of Directors to participate in the Plan.

In consideration of the foregoing and the mutual covenants hereinafter set forth and other good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, the parties hereto agree as follows:

1. Stock Option.

(a) Award. The Company hereby awards to the Grantee, pursuant to the terms and conditions set forth herein, an option to acquire 500,000 shares of Common Stock.

(b) Exercise Price. The exercise price per share of Common Stock payable upon the exercise of the Option is \$2.50. Payment for shares of Common Stock purchased pursuant to an Option shall be made in full upon exercise of the Option. Payment for shares of Common Stock acquired upon exercise of an Option shall be made in cash.

(c) Exercise Date. The Option may be exercised at any time, or from time to time, after the date and to the extent that the Option has vested as provided in Paragraph 2. This Agreement shall not be construed to require the Option rights of the Grantee to be exercisable in installments at fixed intervals.

(d) Expiration. The Option may not be exercised after the date ten years and one day from the Grant Date or, if earlier, after the occurrence of any one of the following events:

(i) ninety (90) days after Grantee's termination of association with the Company, irrespective of whether the termination is voluntary or otherwise, except that the Option exercise period shall not expire (1) in the case of Grantee's total and permanent disability until the determination required in (iii) below shall have been made; or (2) if the Committee of the

Board of Directors of the Company responsible for the administration of the Plan shall in their sole discretion permit exercise of the Option after termination;

(ii) ninety (90) days after Grantee's

normal retirement;

(iii) Grantee's total and permanent disability which, after medical advice, shall be determined by the Board of Directors. The Grantee, or his legal representative, shall have the right at any time within one hundred twenty (120) days after receipt of notice of determination of total and permanent disability to exercise the Option granted hereunder to the extent the Grantee could have exercised such Option immediately before such determination pursuant to the provisions of Paragraph 2; and

(iv) Grantee's death during his association with the Company or any of its subsidiaries, if he shall not have fully exercised any Option awarded hereunder, in which case the same may be exercised at any time within one year after the Grantee's death by the Grantee's personal representative, beneficiary or legal heirs to the extent the Grantee could have exercised such Option immediately before his death pursuant to the provisions of Paragraph 2. The Option shall be exercised only by the Grantee's transferee, who shall be the person or persons entitled to the Option under the Grantee's will, or, if he shall fail to make testamentary disposition of the Option, his legal representative or legal heirs. Any transferee exercising the Option must furnish the Company (1) written notice of his status as transferee; (2) evidence satisfactory to the Company to establish the validity of the transfer of the Option, and compliance with any laws or regulations pertaining to said transfers; and (3) written acceptance by the transferee of the terms and conditions of the Option as prescribed in this Agreement.

(e) Rights of Holder of Option. The Grantee shall have no rights as a shareholder with respect to any share covered by his Option until he shall have become the holder of record of such share, and he shall not be entitled to any dividends or distributions or other rights in respect of such share for which the record date is prior to the date on which he shall have become the holder of record thereof.

2. Vesting Requirements. The Option granted hereunder shall not be exercisable until it has vested. The Option shall vest as follows:

(a) 25% of the shares subject to this Option shall vest immediately following the close of the 12th month following the Grant Date;

(b) an aggregate of 50% of the shares subject to this Option shall vest immediately following the close of the 25th month following the Grant Date;

(c) an aggregate of 75% of the shares subject to this Option shall vest immediately following the close of the 37th month following the Grant Date;

(e) an aggregate of 100% of the shares subject to this Option shall vest

immediately following the close of the 49th month following the Grant Date; and

(f) all of the shares subject to this Option shall vest upon the occurrence of any of the following events:

(i) any Person or Persons acting as a group, become(s) after the date of this Agreement the "beneficial owner" (as defined in Rule 13d-3 under the Securities Exchange Act of 1934, as amended), directly or indirectly, of voting shares (or shares convertible into voting shares) representing 25% or more of the Company's then outstanding voting shares (or shares convertible into voting shares); or

(ii) there shall be a sale of all, or substantially all, of the Company's assets, or the Company shall merge or consolidate with another corporation and the stockholders of the Company immediately prior to such transaction do not own, immediately after such transaction, stock of the purchasing or surviving corporation in this transaction (or of the parent corporation of the purchasing or surviving corporation) possessing more than 50% of the voting power (for the election of Directors) of the outstanding stock of that corporation, which ownership shall be measured without regard to any stock of the purchasing, surviving or parent corporation owned by the stockholders of the Company before the transaction;

provided, however, the provisions of this Section which would otherwise be applicable, shall not apply to a merger or consolidation which does not change any voting securityholder's percentage ownership of the outstanding voting stock in any successor to the Company from the percentage of such stock beneficially owned by such holder in the Company prior to such merger or consolidation, and shall not apply to a transfer of all or substantially all of the assets of the Company to a wholly-owned subsidiary of the Company.

3. Notice of Exercise of Options. Options may be exercised by giving written notice to the Company specifying the number of shares of Common Stock to be purchased accompanied by payment in full of the applicable exercise price. Any written notice to be given to the Company under the terms of this Agreement shall be addressed to the Company, in care of its President, at the Company's then current address. Any written notice to be given to the Grantee shall be addressed to the Grantee at the address set forth by the Grantee in the Grant or as the Grantee may hereafter designate in writing. Any such written notice shall be deemed to have been duly given if and when enclosed in a properly sealed envelope, addressed as aforesaid, registered and deposited, postage prepaid, in a post office or branch post office regularly maintained by the United States Government.

4. Miscellaneous.

(a) Non-Transferability of Awards. Unless otherwise authorized by the Board of Directors or Compensation Committee of the Company, the Option award shall not be transferable except by will or the laws of descent and distribution and during the lifetime of the Grantee, the Option shall be exercised only by him or her or

his legal guardian or legal representative.

(b) Controlling Law. This Agreement shall be subject

to and construed in accordance with the laws of the State of Texas.

(c) Binding Agreement. Subject to the limitations on the transferability of the Option contained herein, this Agreement shall be binding upon and insure to the benefit of the beneficiaries, heirs, legal representatives, successors and assigns of the parties hereto.

IN WITNESS WHEREOF, the parties have executed this Agreement in duplicate to be effective the day and year first above written.

"Company"

"Grantee"

ACCESS PHARMACEUTICALS, INC.

By: /s/ Stephen B. Thompson /s/ Kerry P.Gray

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Stephen B. Thompson Signature  
Treasurer and Chief Financial Officer

4939 Stony Ford Dr.

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Street Address

Dallas, TX 75287

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City, State and Zip code





prior to such redemption date will be payable to the holder of this Security, or one or more predecessor Securities, of record at the close of business on the relevant record dates referred to on the face hereof; provided that this Security may not be redeemed on or after September 30, 2001 unless the Closing Price of the Company Stock exceeds 1.5 times the Conversion Price for any period of 10 consecutive Trading Days commencing on or after August 30, 2001 and ending not less than two Trading Days prior to the Company's giving notice of such redemption to the holder hereof; further provided, that the holder of this Security may extend the Redemption Commencement Date to December 31, 2002 by giving written notice to the Company on or before July 1, 2001 of its election to so extend the Redemption Commencement Date and the Conversion Commencement Date (as defined below).

2. Conversion. (a) The holder of this Security is entitled at any time on or after September 13, 2001 (the "Conversion Commencement Date") and before the close of business on September 13, 2005 (or, in case this Security or a portion hereof is called for redemption or the holder hereof has exercised his right to require the Company to repurchase this Security or a portion hereof, then in respect of this Security or such portion hereof, as the case may be, until and including, but (unless the Company defaults in making the payment due upon redemption or repurchase, as the case may be) not after, the close of business on the redemption date or the Repurchase Date, as the case may be) to convert this Security (or any portion of the principal amount hereof that is an integral multiple of \$5,500), into fully paid and nonassessable shares (calculated as to each conversion to the nearest 1/100 of a share) of Common Stock of the Company at the rate of 1,000 shares of Common Stock (the "Conversion Rate") for each \$5,500 principal amount of Security by surrender of this Security, duly endorsed or assigned to the Company or in blank to the Company at the Designated Office, accompanied by written notice to the Company that the holder hereof elects to convert this Security (or if less than the entire principal amount hereof is to be converted, specifying the portion hereof to be converted) provided, that the holder of this Security may extend the Conversion Commencement Date to December 13, 2002 by giving written notice to the Company on or before July 1, 2001 of its election to so extend the Conversion Commencement Date and Redemption Commencement Date. Upon surrender of this Security for conversion, the holder will be entitled to receive the interest accruing on the principal amount of this Security then being converted from the interest payment date next preceding the date of such conversion to such date of conversion. No payment or adjustment is to be made on conversion for dividends on the Common Stock issued on conversion hereof. No fractions of shares or scrip representing fractions of shares will be

2

issued on conversion, but instead of any fractional interest, the Company shall pay a cash adjustment, computed on the basis of the Closing Price of the Common Stock on the date of conversion, or, at its option, the Company shall round up to the next higher whole share.

(b) The Conversion Rate shall be subject to adjustments from time to time as follows:

(1) In case the Company shall pay or make a dividend or other distribution on any class of capital stock of the Company payable in shares of Common Stock, the Conversion Rate in effect at the opening of business on the day following the Determination Date for such dividend or other distribution shall be increased by dividing such Conversion Rate by a fraction of which the numerator shall be the number of shares of Common Stock outstanding at the close of business on such Determination Date and the denominator shall be the sum of such number of shares and the total number of shares constituting such dividend or other distribution, such increase to become effective immediately after the opening of business on the day following such Determination Date. For the purposes of this paragraph (1), the number of shares of Common Stock at any time outstanding shall not include shares held in the treasury of the Company but shall include shares issuable in respect of scrip certificates issued in lieu of fractions of

shares of Common Stock.

(2) Subject to the last sentence of paragraph (7) of this Section 2(b), in case the Company shall issue rights, options or warrants to all holders of its Common Stock entitling them to subscribe for or purchase shares of Common Stock at a price per share less than the current market price per share (determined as provided in paragraph (8) of this Section 2(b)) of the Common Stock on the Determination Date for such distribution, the Conversion Rate in effect at the opening of business on the day following such Determination Date shall be increased by dividing such Conversion Rate by a fraction of which the numerator shall be the number of shares of Common Stock outstanding at the close of business on such Determination Date plus the number of shares of Common Stock which the aggregate of the offering price of the total number of shares of Common Stock so offered for subscription or purchase would purchase at such current market price and the denominator shall be the number of shares of Common Stock outstanding at the close of business on such Determination Date plus the number of shares of Common Stock so offered for subscription or purchase, such increase to become effective immediately after the opening of business on the day following such Determination Date. For the purposes of this paragraph (2), the number of shares of Common Stock at any time outstanding shall not include shares held in the treasury of the Company but shall include shares issuable in respect of scrip certificates issued in lieu of fractions of shares of Common Stock.

(3) In case outstanding shares of Common Stock shall be subdivided into a greater number of shares of Common Stock, the Conversion Rate in effect at the opening of business on the day following the day upon which such subdivision becomes effective shall be proportionately increased, and, conversely, in case outstanding shares of Common Stock shall each be combined into a smaller number of shares of Common

3

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Rate in effect at the opening of business on the day following the day upon which such combination becomes effective shall be proportionately reduced, such increase or reduction, as the case may be, to become effective immediately after the opening of business on the day following the day upon which such subdivision or combination becomes effective.

(4) Subject to the last sentence of paragraph (7) of this Section 2(b), in case the Company shall, by dividend or otherwise, distribute to all holders of its Common Stock evidences of its indebtedness, shares of any class of capital stock, or other property (including securities, but excluding (i) any rights, options or warrants referred to in paragraph (2) of this Section 2(b), (ii) any dividend or distribution paid exclusively in cash, (iii) any dividend or distribution referred to in paragraph (1) of this Section 2(b) and (iv) any merger or consolidation to which Section 2(h) applies), the Conversion Rate shall be adjusted so that the same shall equal the rate determined by dividing the Conversion Rate in effect immediately prior to the close of business on the Determination Date for such distribution by a fraction of which the numerator shall be the current market price per share (determined as provided in paragraph (8) of this Section 2(b)) of the Common Stock on such Determination Date less the then fair market value (as determined in good faith by the Board of Directors of the Company) of the portion of the assets, shares or evidences of indebtedness so distributed applicable to one share of Common Stock and the denominator shall be such current market price per share of the Common Stock, such adjustment to become effective immediately prior to the opening of business on the day following such Determination Date. If the Board of Directors determines the fair market value of any distribution for purposes of this paragraph (4) by reference to the actual or when issued trading market for any securities comprising such distribution, it must in doing so consider the prices in such market over the same period used in computing the current market price per share pursuant to

paragraph (8) of this Section 2(b).

(5) In case the Company shall, by dividend or otherwise, make a Cash Distribution, then, and in each such case, immediately after the close of business on the Determination Date for such Cash Distribution, the Conversion Rate shall be adjusted so that the same shall equal the rate determined by dividing the Conversion Rate in effect immediately prior to the close of business on such Determination Date by a fraction (a) the numerator of which shall be equal to the current market price per share (determined as provided in paragraph (8) of this Section 2(b)) of the Common Stock on such Determination Date less an amount equal to the quotient of (1) the amount of such Cash Distribution divided by (2) the number of shares of Common Stock outstanding on such Determination Date and (b) the denominator of which shall be equal to the current market price per share (determined as provided in paragraph (8) of this Section 2(b)) of the Common Stock on such Determination Date.

(6) In case the Company or any Subsidiary shall make an Excess Purchase Payment, then, and in each such case, immediately prior to the opening of business on the day after the tender offer in respect of which such Excess Purchase Payment is to be made expires, the Conversion Rate shall be adjusted so that the same shall equal the rate

4

determined by dividing the Conversion Rate in effect immediately prior to the close of business on the Determination Date for such tender offer by a fraction (a) the numerator of which shall be equal to the current market price per share (determined as provided in paragraph (8) of this Section 2(b)) of the Common Stock at such Determination Date less the amount of such Excess Purchase Payment and (b) the denominator of which shall be equal to the current market price per share of the Common Stock (determined as provided in paragraph (8) of this Section 2(b)) as of such Determination Date.

(7) The reclassification of Common Stock into securities other than Common Stock (other than any reclassification upon a consolidation or merger to which Section 2(h) applies) shall be deemed to involve (a) a distribution of such securities other than Common Stock to all holders of Common Stock (and the effective date of such reclassification shall be deemed to be the Determination Date), and (b) a subdivision or combination, as the case may be, of the number of shares of Common Stock outstanding immediately prior to such reclassification into the number of shares of Common Stock outstanding immediately thereafter (and the effective date of such reclassification shall be deemed to be "the day upon which such subdivision becomes effective" or "the day upon which such combination becomes effective", as the case may be, and "the day upon which such subdivision or combination becomes effective" within the meaning of paragraph (3) of this Section 2(b)). Rights or warrants issued by the Company to all holders of its Common Stock entitling the holders thereof to subscribe for or purchase shares of Common Stock, which rights or warrants (i) are deemed to be transferred with such shares of Common Stock, (ii) are not exercisable and (iii) are also issued in respect of future issuances of Common Stock, in each case in clauses (i) through (iii) until the occurrence of a specified event or events ("Trigger Event"), shall for purposes of this Section 2(b) not be deemed issued until the occurrence of the earliest Trigger Event.

(8) For the purpose of any computation under paragraphs (2), (4), (5) or (6) of this Section 2(b) the current market price per share of Common Stock on any date shall be calculated by the Company and be deemed to be the average of the daily Closing Prices for the five consecutive Trading Days selected by the Company commencing not more than 10 Trading Days before, and ending not later than, the earlier of the day in question and the day before the "ex" date with respect to the issuance or distribution requiring such computation. For purposes of this paragraph, the

term "ex date", when used with respect to any issuance or distribution, means the first date on which the Common Stock trades regular way in the applicable securities market or on the applicable securities exchange without the right to receive such issuance or distribution.

(9) No adjustment in the Conversion Rate shall be required unless such adjustment (plus any adjustments not previously made by reason of this paragraph (9)) would require an increase or decrease of at least one percent in such rate; provided, however, that any adjustments which by reason of this paragraph (9) are not required to be made shall be carried forward and taken into account in any subsequent adjustment. All calculations under this Section 2 shall be made to the nearest cent or to the nearest one-hundredth of a share, as the case may be.

5

(10) The Company may make such increases in the Conversion Rate, for the remaining term of the Securities or any shorter term, in addition to those required by paragraphs (1), (2), (3), (4), (5) and (6) of this Section 2(b) as it considers to be advisable in order to avoid or diminish any income tax to any holders of shares of Common Stock resulting from any dividend or distribution of stock or issuance of rights or warrants to purchase or subscribe for stock or from any event treated as such for income tax purposes.

(c) Whenever the Conversion Rate is adjusted as provided in Section 2(b), the Company shall compute the adjusted Conversion Rate in accordance with Section 2(b) and shall prepare a certificate signed by the chief financial officer of the Company setting forth the adjusted Conversion Rate and showing in reasonable detail the facts upon which such adjustment is based, and shall promptly deliver such certificate to the holder of Security.

(d) In case:

(1) the Company shall declare a dividend or other distribution on its Common Stock payable (i) otherwise than exclusively in cash or (ii) exclusively in cash in an amount that would require any adjustment pursuant to Section 2(b); or

(2) the Company shall authorize the granting to the holders of its Common Stock of rights, options or warrants to subscribe for or purchase any shares of capital stock of any class or of any other rights; or

(3) of any reclassification of the Common Stock of the Company, or of any consolidation, merger or share exchange to which the Company is a party and for which approval of any shareholders of the Company is required, or of the conveyance, sale, transfer or lease of all or substantially all of the assets of the Company; or

(4) of the voluntary or involuntary dissolution, liquidation or winding up of the Company; or

(5) the Company or any Subsidiary shall commence a tender offer for all or a portion of the Company's outstanding shares of Common Stock (or shall amend any such tender offer);

then the Company shall cause to be delivered to the holder of this Security, at least 10 days prior to the applicable record, expiration or effective date hereinafter specified, a notice stating (x) the date on which a record is to be taken for the purpose of such dividend, distribution, rights, options or warrants, or, if a record is not to be taken, the date as of which the holders of Common Stock of record to be entitled to such dividend, distribution, rights, options or warrants are to be determined, (y) the date on which the right to make tenders under such tender offer expires or (z) the date on which such reclassification, consolidation,

merger, conveyance, transfer, sale, lease, dissolution, liquidation or winding up is expected to become effective, and the date as of which it

6

is expected that holders of Common Stock of record shall be entitled to exchange their shares of Common Stock for securities, cash or other property deliverable upon such reclassification, consolidation, merger, conveyance, transfer, sale, lease, dissolution, liquidation or winding up. Neither the failure to give such notice nor any defect therein shall affect the legality or validity of the proceedings described in clauses (1) through (5) of this Section 2(d).

(e) The Company shall at all times reserve and keep available, free from preemptive rights, out of its authorized but unissued Common Stock, for the purpose of effecting the conversion of the Security, the full number of shares of Common Stock then issuable upon the conversion of this Security.

(f) Except as provided in the next sentence, the Company will pay any and all stamp or transfer taxes and duties that may be payable in respect of the issue or delivery of shares of Common Stock on conversion of the Security. The Company shall not, however, be required to pay any tax or duty which may be payable in respect of any transfer involved in the issue and delivery of shares of Common Stock in a name other than that of the holder of this Security, and no such issue or delivery shall be made unless and until the person requesting such issue has paid to the Company the amount of any such tax or duty, or has established to the satisfaction of the Company that such tax or duty has been paid.

(g) The Company agrees that all shares of Common Stock which may be delivered upon conversion of the Security, upon such delivery, will have been duly authorized and validly issued and will be fully paid and nonassessable (and shall be issued out of the Company's authorized but unissued Common Stock) and, except as provided in Section 2(f), the Company will pay all stamp or transfer taxes, liens and charges with respect to the issue thereof.

(h) In case of any consolidation of the Company with any other person, any merger of the Company into another person or of another person into the Company (other than a merger which does not result in any reclassification, conversion, exchange or cancellation of outstanding shares of Common Stock of the Company) or any conveyance, sale, transfer or lease of all or substantially all of the properties and assets of the Company, the person formed by such consolidation or resulting from such merger or which acquires such properties and assets, as the case may be, shall execute and deliver to the holder of this Security a supplemental agreement providing that such holder have the right thereafter, during the period this Security shall be convertible as specified in Section 2(a), to convert this Security only into the kind and amount of securities, cash and other property receivable upon such consolidation, merger, conveyance, sale, transfer or lease (including any Common Stock retainable) by a holder of the number of shares of Common Stock of the Company into which this Security might have been converted immediately prior to such consolidation, merger, conveyance, sale, transfer or lease, assuming such holder of Common Stock of the Company (i) is not a person with which the Company consolidated, into which the Company merged or which merged into the Company or to which such conveyance, sale, transfer or lease was made, as the case may be (a "Constituent Person"), or an Affiliate of a Constituent Person and (ii) failed to exercise his rights of election, if any, as to the kind or amount of securities, cash and other property receivable upon such consolidation, merger, conveyance, sale, transfer or lease (provided that if the kind or amount of securities, cash and other property receivable upon such consolidation, merger, conveyance, sale, transfer, or

7

lease is not the same for each share of Common Stock of the Company held immediately prior to such consolidation, merger, conveyance, sale, transfer or lease by others than a Constituent Person or an Affiliate thereof and in respect of which such rights of election shall not have been exercised ("Non-electing Share"),

then for the purpose of this Section 2(h) the kind and amount of securities, cash and other property receivable upon such consolidation, merger, conveyance, sale, transfer or lease by the holders of each Non-electing Share shall be deemed to be the kind and amount so receivable per share by a plurality of the Non-electing Shares). Such supplemental agreement shall provide for adjustments which, for events subsequent to the effective date of such supplemental agreement, shall be as nearly equivalent as may be practicable to the adjustments provided for in this Section 2. The above provisions of this Section 2(h) shall similarly apply to successive consolidations, mergers, conveyances, sales, transfers or leases. In this paragraph, "securities of the kind receivable" upon such consolidation, merger, conveyance, transfer, sale or lease by a holder of Common Stock means securities that, among other things, are registered and transferable under the Securities Act, and listed and approved for quotation in all securities markets, in each case to the same extent as such securities so receivable by a holder of Common Stock.

(i) The Company (a) will effect all registrations with, and obtain all approvals by, all governmental authorities that may be necessary under any United States Federal or state law (including the Securities Act of 1933, as amended (the "Securities Act"), the Securities Exchange Act of 1934, as amended, and state securities and Blue Sky laws) for the shares of Common Stock issuable upon conversion of this Security to be lawfully issued and delivered as provided herein, and thereafter publicly traded (if permissible under such Securities Act) and qualified or listed as contemplated by clause (b) below (it being understood that the Company shall not be required to register the Common Stock issuable on conversion hereof under the Securities Act, except pursuant to the Registration Rights Agreement between the Company and the initial holder of this Security); and (b) will list the shares of Common Stock required to be issued and delivered upon conversion of Securities, prior to such issuance or delivery, on each national securities exchange on which outstanding Common Stock is listed or quoted at the time of such delivery, or if the Common Stock is not then listed on any securities exchange, to qualify the Common Stock for quotation on the Nasdaq National Market or such other inter-dealer quotation system, if any, on which the Common Stock is then quoted.

(j) For purposes hereof:

"Affiliate" of any specified person means any other person directly or indirectly controlling or controlled by or under direct or indirect common control with such specified person. For the purposes of this definition, "control", when used with respect to any specified person, means the power to direct the management and policies of such person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise; and the terms "controlling" and "controlled" have meanings correlative to the foregoing.

"Cash Distribution" means the distribution by the Company to all holders of its Common Stock of cash, other than any cash that is distributed upon a merger or consolidation to which Section 2(h) applies or as part of a distribution referred to in paragraph (4) of Section 2(b).

8

"Closing Price" means, with respect to the Common Stock of the Company, for any day, the reported last sale price per share on the American Stock Exchange, or, if the Common Stock is not admitted to trading on the American Stock Exchange, on the principal national securities exchange or inter-dealer quotation system on which the Common Stock is listed or admitted to trading, or if not admitted to trading on the Nasdaq National Market, or listed or admitted to trading on any national securities exchange or inter-dealer quotation system, the average of the closing bid and asked prices per share in the over-the-counter market as furnished by any New York Stock Exchange member firm selected from time to time by the Company for that purpose.

"Common Stock" means the Common Stock, par value \$.01 per share, of the Company authorized at the date of this instrument as originally executed. Subject to the provisions of Section 2(h), shares issuable on conversion or repurchase of this Security shall include only shares of Common Stock or shares of any class or classes of common

stock resulting from any reclassification or reclassifications thereof; provided, however, that if at any time there shall be more than one such resulting class, the shares so issuable on conversion of this Security shall include shares of all such classes, and the shares of each such class then so issuable shall be substantially in the proportion which the total number of shares of such class resulting from all such reclassifications bears to the total number of shares of all such classes resulting from all such reclassifications.

"Conversion Price" on any day means an amount equal to \$5,500 divided by the Conversion Rate in effect on such day.

"Determination Date" means, in the case of a dividend or other distribution, including the issuance of rights, options or warrants, to shareholders, the date fixed for the determination of shareholders entitled to receive such dividend or other distribution and, in the case of a tender offer, the last time that tenders could have been made pursuant to such tender offer.

"Excess Purchase Payment" means the excess, if any, of (i) the amount of cash plus the fair market value (as determined in good faith by the Company's Board of Directors) of any non-cash consideration required to be paid with respect to one share of Common Stock acquired or to be acquired in a tender offer made by the Company or any subsidiary of the Company for all or any portion of the Common Stock over (ii) the current market price per share as of the last time that tenders could have been made pursuant to such tender offer.

"Trading Day" means (i) if the Common Stock is listed or admitted for trading on the New York or American Stock Exchange or any other national securities exchange, a day on which such exchange is open for business; (ii) if the Common Stock is admitted to trading on the Nasdaq National Market or any other system of automated dissemination of quotations of securities prices, a day on which trades may be effected through such system; or (iii) if the Common Stock is not admitted to trading on the Nasdaq National Market or listed or admitted for trading on any national securities exchange or any other system of automated dissemination of quotation of securities prices, a day on which the Common Stock is traded regular way in the

over-the-counter market and for which a closing bid and a closing asked price for the Common Stock are available.

3. Right to Require Repurchase. (a) In the event that a Change in Control (as hereinafter defined) shall occur, then the holder of this Security shall have the right, at such holder's option, subject to the rights of holders of Senior Indebtedness, to require the Company to repurchase, and upon the exercise of such right the Company shall repurchase, this Security, or any portion of the principal amount hereof that is equal to \$5,500 or any integral multiple thereof, on the date (the "Repurchase Date") that is ten Trading Days after the date on which the Company gives notice thereof to the holder of this Security, at a purchase price equal to 105% of the principal amount of this Security to be repurchased, plus interest accrued to the Repurchase Date (the "Repurchase Price"); provided, however, that installments of interest on this Security whose stated maturity is on or prior to the Repurchase Date shall be payable to the holder of this Security, or one or more predecessor Securities, registered as such on the relevant Record Date according to their terms. Upon surrender of this Security for repurchase, the holder will be entitled to receive the interest accruing on the principal amount of this Security then being repurchased from the interest payment date next preceding the date of such repurchase to such date of repurchase. At the option of the Company, the Repurchase Price may be paid in cash or, subject to the fulfillment by the Company of the conditions set forth in Section 3(b), by delivery of shares of Common Stock having a fair market value equal to the Repurchase Price as described in Section 3(b). The Company agrees to give the holder of this Security notice of any Change in Control, by facsimile transmission confirmed in writing by overnight courier service, promptly and in any event within two Trading Days of the occurrence thereof.

(b) The Company may elect to pay the Repurchase Price by delivery of shares of Common Stock pursuant to Section 3(a), if and only if the following conditions have been satisfied:

(1) The shares of Common Stock deliverable in payment of the Repurchase Price shall have a fair market value as of the Repurchase Date of not less than the Repurchase Price. For purposes of this Section 3(b), the fair market value of shares of Common Stock shall be equal to 95% of the average of the Closing Prices for the five consecutive Trading Days ending on and including the third Trading Day immediately preceding the Repurchase Date;

(2) In the event any shares of Common Stock to be issued upon repurchase of this Security require registration under any Federal securities law before such shares may be freely transferable without being subject to any transfer restrictions under the Securities Act of 1933 upon issuance, such registration shall have been completed and shall have become effective prior to the Repurchase Date;

(3) In the event any shares of Common Stock to be issued upon repurchase of this Security require registration with or approval of any governmental authority under any State law or any other Federal law before such shares may be validly issued or delivered upon repurchase, such registration shall have been completed, have become effective and such approval shall have been obtained, in each case, prior to the Repurchase Date;

10

(4) Immediately prior to the Repurchase Date the shares of Common Stock deliverable in payment of the Repurchase Price shall have been approved for trading or listed on the American Stock Exchange or the principal national securities exchange or interdealer quotation system on which the Common Stock is then admitted to trading or listed; and

(5) All shares of Common Stock deliverable in payment of the Repurchase Price shall be issued out of the Company's authorized but unissued Common Stock and will, upon issue, be duly and validly issued and fully paid and non-assessable and free of any preemptive rights.

If all of the conditions set forth in this Section 3(b) are not satisfied in accordance with the terms thereof, the Repurchase Price shall be paid by the Company only in cash.

(c) To exercise a repurchase right, the holder shall deliver to the Company on or before the 5th day prior to the Repurchase Date, together with this Security, written notice of the holder's exercise of such right, which notice shall set forth the name of the holder, the principal amount of this Security to be repurchased (and, if this Security is to be repurchased in part, the portion of the principal amount thereof to be repurchased and the name of the person in which the portion thereof to remain outstanding after such repurchase is to be registered) and a statement that an election to exercise the repurchase right is being made thereby, and, in the event that the Repurchase Price shall be paid in shares of Common Stock, the name or names (with addresses) in which the certificate or certificates for shares of Common Stock shall be issued. Such written notice shall be irrevocable, except that the right of the holder to convert this Security (or the portion hereof with respect to which the repurchase right is being exercised) shall continue until the close of business on the Repurchase Date.

(d) In the event a repurchase right shall be exercised in accordance with the terms hereof, the Company shall pay or cause to be paid to the holder the Repurchase Price in cash or shares of Common Stock, as provided above, or, if shares of Common Stock are to be paid, as promptly after the Repurchase Date as practicable, together with accrued and unpaid interest to the Repurchase Date; provided, however, that installments of interest that mature on or prior to the Repurchase Date shall be payable in cash, to the holders of this Security, or one or more predecessor Securities, registered as such at the close of business on the relevant regular record date.

(e) If this Security (or portion thereof) is surrendered for



repurchase and is not so paid on the Repurchase Date, the principal amount of this Security (or such portion hereof, as the case may be) shall, until paid, bear interest to the extent permitted by applicable law from the Repurchase Date at the rate per annum borne by this Security, and shall remain convertible into Common Stock until the principal of this Security (or portion thereof, as the case may be) shall have been paid or duly provided for.

(f) If this Security is to be repurchased only in part, it shall be surrendered to the Company at the Designated Office (with, if the Company so requires, due endorsement by, or a written instrument of transfer in form satisfactory to the Company duly executed by, the holder hereof or his attorney duly authorized in writing), and the Company shall execute and make

11

available for delivery to the holder without service charge, a new Security or Securities, containing identical terms and conditions, each in an authorized denomination in aggregate principal amount equal to and in exchange for the unrepurchased portion of the principal of the Security so surrendered.

(g) Any issuance of shares of Common Stock in respect of the Repurchase Price shall be deemed to have been effected immediately prior to the close of business on the Repurchase Date and the person or persons in whose name or names any certificate or certificates for shares of Common Stock shall be issuable upon such repurchase shall be deemed to have become on the Repurchase Date the holder or holders of record of the shares represented thereby; provided, however, that any surrender for repurchase on a date when the stock transfer books of the Company shall be closed shall constitute the person or persons in whose name or names the certificate or certificates for such shares are to be issued as the record holder or holders thereof for all purposes at the opening of business on the next succeeding day on which such stock transfer books are open. No payment or adjustment shall be made for dividends or distributions on any Common Stock issued upon repurchase of this Security declared prior to the Repurchase Date.

(h) No fractions of shares shall be issued upon repurchase of this Security. Instead of any fractional share of Common Stock which would otherwise be issuable on the repurchase of this Security, the Company will deliver to the holder its check for the current market value of such fractional share. The current market value of a fraction of a share shall be determined by multiplying the current market price of a full share by the fraction, and rounding the result to the nearest cent. For purposes of this Section 3 the current market price of a share of Common Stock shall be the Closing Price of the Common Stock on the Trading Day immediately preceding the Repurchase Date.

(i) Any issuance and delivery of certificates for shares of Common Stock on repurchase of this Security shall be made without charge to the holder of this Security for such certificates or for any stamp or transfer tax or duty in respect of the issuance or delivery of such certificates or the securities represented thereby; provided, however, that the Company shall not be required to pay any tax or duty which may be payable in respect of any transfer involved in the issuance or delivery of certificates for shares of Common Stock in a name other than that of the holder of this Security, and no such issuance or delivery shall be made unless and until the person requesting such issuance or delivery has paid to the Company the amount of any such tax or duty or has established, to the satisfaction of the Company, that such tax or duty has been paid.

(j) For purposes of this Section 3;

(1) the term "beneficial owner" shall be determined in accordance with Rule 13d-3 promulgated by the Securities and Exchange Commission pursuant to the Securities Exchange Act of 1934; and

(2) a "Change in Control" shall be deemed to have occurred at the time, after the original issuance of this Security, of:

12

(i) the acquisition by any person of beneficial ownership, directly or indirectly, through a purchase, merger or other acquisition transaction or series of transactions, of shares of capital stock of the Company entitling such person to exercise 50% or more of the total voting power of all shares of capital stock of the Company entitled to vote generally in the election of directors (any shares of voting stock of which such person is the beneficial owner that are not then outstanding being deemed outstanding for purposes of calculating such percentage) other than any such acquisition by the Company or any employee benefit plan of the Company;

(ii) any consolidation or merger of the Company with or into, any other person, any merger of another person with or into the Company, or any conveyance, transfer, sale, lease or other disposition of all or substantially all of the assets of the Company to another person (other than (a) any such transaction (x) which does not result in any reclassification, conversion, exchange or cancellation of outstanding shares of Common Stock and (y) pursuant to which holders of Common Stock immediately prior to such transaction have the entitlement to exercise, directly or indirectly, 50% or more of the total voting power of all shares of capital stock entitled to vote generally in the election of directors of the continuing or surviving person immediately after such transaction and (b) any merger which is effected solely to change the jurisdiction of incorporation of the Company and results in a reclassification, conversion or exchange of outstanding shares of Common Stock solely into shares of common stock);

provided, however, that a Change in Control shall not be deemed to have occurred if the Closing Price for any five Trading Days within the period of 10 consecutive Trading Days (x) ending immediately after the later of the date of the Change in Control or the date of the public announcement of the Change in Control (in the case of a Change in Control under Clause (i) above) or (y) ending immediately prior to the date of the Change in Control (in the case of a Change in Control under Clause (ii) above) shall equal or exceed 105% of the Conversion Price in effect on each such Trading Day.

4. Events of Default. (a) "Event of Default", wherever used herein, means any one of the following events (whatever the reason for such Event of Default and whether it shall be occasioned by the provisions of Section 6 or be voluntary or involuntary or be effected by operation of law or pursuant to any judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body):

(1) default in the payment of any interest upon this Security when it becomes due and payable, and continuance of such default for a period of 30 days; or

(2) default by the Company in the performance of its obligations in respect of any conversion of this Security (or any portion hereof) in accordance with Section 2; or

(3) failure by the Company to give any notice of a Change of Control required to be delivered in accordance with Section 3(a); or

13

(4) default in the performance, or breach, of any material covenant or warranty of the Company herein (other than a covenant or warranty a default in the performance or breach of which is specifically dealt with elsewhere in this Section 4(a)) and continuance of such default or breach for a period of 30 days after there has been given, by registered or certified mail, to the Company by the holder of this Security a written notice specifying such default or breach and requiring it to be remedied and stating that such notice is a "Notice of Default" hereunder; or

(5) a default under any bond, debenture, note or other

evidence of indebtedness for money borrowed by the Company, or under any agreement, mortgage, indenture or instrument under which there may be issued or by which there may be secured or evidenced any indebtedness for money borrowed by the Company, with a principal amount then outstanding in excess of \$1,000,000, whether such indebtedness now exists or shall hereafter be created, which default shall constitute a failure to pay the principal of such indebtedness (in whole or in any part greater than \$1,000,000) when due and payable or shall have resulted in such indebtedness (in whole or in any part greater than \$1,000,000) becoming or being declared due and payable prior to the date on which it would otherwise have become due and payable, without such indebtedness having been discharged, or such acceleration having been rescinded or annulled, within a period of 30 days after there shall have been given, by registered or certified mail, to the Company by the holder of this Security a written notice specifying such default and requiring the Company to cause such indebtedness to be discharged or cause such acceleration to be rescinded or annulled and stating that such notice is a "Notice of Default" hereunder; or

(6) the entry by a court having jurisdiction in the premises of (i) a decree or order for relief in respect of the Company in an involuntary case or proceeding under any applicable Federal or state bankruptcy, insolvency, reorganization or other similar law or (ii) a decree or order adjudging the Company bankrupt or insolvent, or approving as properly filed a petition seeking reorganization, arrangement, adjustment or composition of or in respect of the Company under any applicable Federal or state law, or appointing a custodian, receiver, liquidator, assignee, trustee, sequestrator or other similar official of the Company or of any substantial part of its property, or ordering the winding up or liquidation of its affairs, and the continuance of any such decree or order for relief or any such other decree or order unstayed and in effect for a period of 60 consecutive days; or

(7) the commencement by the Company of a voluntary case or proceeding under any applicable Federal or State bankruptcy, insolvency, reorganization or other similar law or of any other case or proceeding to be adjudicated a bankrupt or insolvent, or the consent by it to the entry of a decree or order for relief in respect of the Company in an involuntary case or proceeding under any applicable Federal or State bankruptcy, insolvency, reorganization or other similar law or to the commencement of any bankruptcy or insolvency case or proceeding against it, or the filing by it of a petition or answer or consent seeking reorganization or similar relief under any applicable Federal or State law, or the consent by it to the filing of such petition or to the appointment of or taking possession by a custodian, receiver, liquidator, assignee, trustee, sequestrator or other similar official of the Company or of any substantial part of its property, or the

14

making by it of an assignment for the benefit of creditors, or the admission by it in writing of its inability to pay its debts generally as they become due, or the taking of corporate action by the Company in furtherance of any such action.

(b) If an Event of Default (other than an Event of Default specified in Section 4(a)(6) or 4(a)(7)) occurs and is continuing, then in every such case the holder of this Security may declare the principal hereof to be due and payable immediately, by a notice in writing to the Company, and upon any such declaration such principal and all accrued interest thereon shall become immediately due and payable. If an Event of Default specified in Section 4(a)(6) or 4(a)(7) occurs and is continuing, the principal of, and accrued interest on, this Security shall ipso facto become immediately due and payable without any declaration or other act of the holders.

5. Consolidation, Merger, Etc. (a) The Company shall not consolidate with or merge into any other person or, directly or

indirectly, convey, transfer, sell or lease all or substantially all of its properties and assets to any person, and the Company shall not permit any person to consolidate with or merge into the Company or, directly or indirectly, convey, transfer, sell or lease all or substantially all of its properties and assets to the Company, unless:

(1) in case the Company shall consolidate with or merge into another person or convey, transfer, sell or lease all or substantially all of its properties and assets to any person, the person formed by such consolidation or into which the Company is merged or the person which acquires by conveyance, transfer or sale, or which leases, all or substantially all the properties and assets of the Company shall be a corporation, limited liability company, partnership or trust, shall be organized and validly existing and shall expressly assume, by an agreement supplemental hereto, executed and delivered to the holder of this Security, the due and punctual payment of the principal of and interest on this Security and the performance or observance of every covenant of this Security on the part of the Company to be performed or observed, including the conversion rights provided herein;

(2) immediately after giving effect to such transaction and treating any indebtedness which becomes an obligation of the Company or a subsidiary of the Company as a result of such transaction as having been incurred by the Company or such subsidiary of the Company at the time of such transaction, no Event of Default, and no event which, after notice or lapse of time or both, would become an Event of Default, shall have happened and be continuing; and

(3) the Company has delivered to the holder of this Security an officers' certificate stating that such consolidation, merger, conveyance, transfer, sale or lease and, if a supplemental agreement is required in connection with such transaction, such supplemental agreement, comply with this Section and that all conditions precedent herein provided for relating to such transaction have been complied with.

(b) Upon any consolidation of the Company with, or merger of the Company into, any other person or any conveyance, transfer, sale or lease of all or substantially all of the

15

properties and assets of the Company in accordance with Section 5(a), the successor person formed by such consolidation or into which the Company is merged or to which such conveyance, transfer, sale or lease is made shall succeed to, and be substituted for, and may exercise every right and power of, the Company under this Security with the same effect as if such successor person had been named as the Company herein, and thereafter, except in the case of a lease, the predecessor person shall be relieved of all obligations and covenants under this Security.

6. Subordination. The Company agrees, and the holder of this Security by accepting a Security agrees, that the indebtedness evidenced by this Security is subordinated in right of payment to the prior payment in full of all Senior Indebtedness, and that the subordination is for the benefit of the holders of Senior Indebtedness.

"Senior Indebtedness" means:

(a) the principal of, interest (including, to the extent permitted by applicable law, interest on or after the commencement of any bankruptcy or similar proceeding whether or not representing an allowed claim in such proceeding) on and any other amounts owing with respect to (i) any indebtedness of the Company, now or hereafter outstanding, in respect of borrowed money (other than the Securities), (ii) any indebtedness of the Company, now or hereafter outstanding, evidenced by a bond, note, debenture, capitalized lease, letter of credit or other similar instrument, (iii) any other written obligation of the Company, now or hereafter outstanding, to pay money issued or assumed as all or part of the consideration for the acquisition of property, assets or securities and (iv) any guaranty or endorsement (other than for collection or deposit in

the ordinary course of business) or discount with recourse of, or other agreement (contingent or otherwise) to purchase, repurchase or otherwise acquire, to supply or advance funds or to become liable with respect to (directly or indirectly), any indebtedness or obligation of any person of the type referred to in the preceding subclauses (i), (ii) and (iii) now or hereafter outstanding; and

(b) any refundings, renewals or extensions of any indebtedness or other obligation described in clause (a) above.

Notwithstanding the foregoing, if, by the terms of the instrument creating or evidencing any indebtedness or obligation referred to in clauses (a) and (b) above, it is expressly provided that such indebtedness or obligation is not senior in right of payment to this Security, such indebtedness or obligation shall not be included as Senior Indebtedness.

7. Other. (a) No provision of this Security shall alter or impair the obligation of the Company, which is absolute and unconditional, to pay the principal of, premium, if any, and interest on this Security at the times, places and rate, and in the coin or currency, herein prescribed or to convert this Security as herein provided.

(b) The Company will give prompt written notice to the holder of this Security of any change in the location of the Designated Office.

16

(c) The transfer of this Security is registrable on the Security Register of the Company upon surrender of this Security for registration of transfer at the Designated Office, duly endorsed by, or accompanied by a written instrument of transfer in form satisfactory to the Company duly executed by, the holder hereof or his attorney duly authorized in writing, and thereupon one or more new Securities, of authorized denominations and for the same aggregate principal amount, will be issued to the designated transferee or transferees. Such Securities are issuable only in registered form without coupons in denominations of \$5,500 and any integral multiple thereof. No service charge shall be made for any such registration of transfer, but the Company may require payment of a sum sufficient to recover any tax or other governmental charge payable in connection therewith. Prior to due presentation of this Security for registration of transfer, the Company and any agent of the Company may treat the person in whose name this Security is registered, as the owner thereof for all purposes, whether or not this Security be overdue, and neither the Company, nor any such agent shall be affected by notice to the contrary.

Notwithstanding any other provision of this Security, this Security and the shares of Common Stock issuable upon conversion hereof may only be transferred by the holder of this Security (a) in the case of the Common Stock only, in a public offering registered under the Securities Act of 1933, as amend; (b) to one or more investors, in one or more transactions, any one of whom, after such purchase, would hold not more than 5% of the shares of Common Stock then outstanding (assuming conversion of any portion of this Security so transferred); (c) to any person or entity that already controls more than 50% of the voting securities of the Company prior to such transfer; (d) in a transaction that complies with the manner of sale restrictions of Rule 144 under the Securities Act; or (e) in a transaction approved in advance by the Federal Reserve Board. The holder of this Security, by acceptance thereof, shall be deemed to have agreed to the foregoing restriction on transfers.

(d) The holder agrees that, at the written request of the Company or any managing underwriter of any underwritten public offering of securities of the Company, such holder shall not, without the prior written consent of the Company or such managing underwriter, sell, make any short sale of, loan, grant any option for the purchase of, pledge, encumber, or otherwise dispose of, or exercise any registration rights with respect to, any Securities or Common Stock of the Company during the 180-day period commencing on the effective date of the registration statement relating to such underwritten public offering of the Company's securities; provided, that each officer and director of the Company shall

have entered into a similar agreement.

(e) This Security shall be governed by and construed in accordance with the laws of the State of Texas, United States of America.

17

IN WITNESS WHEREOF, the Company has caused this Security to be duly executed under its corporate seal.

Dated:

By: \_\_\_\_\_  
Name: Kerry P.Gray  
Title: Chief Executive Officer

Attest:

\_\_\_\_\_  
Name:

18

ELECTION OF HOLDER TO REQUIRE REPURCHASE

1. Pursuant to Section 3(a) of this Security, the undersigned hereby elects to have all or a portion of this Security repurchased by the Company.

2. The undersigned hereby directs the Company to pay [choose one] (a) it or (b) Name: \_\_\_\_\_; address: \_\_\_\_\_; Social Security or Other Taxpayer Identification Number, if any: \_\_\_\_\_, an amount in cash or, at the Company's election, Common Stock valued as set forth in the Security, equal to 100% of the principal amount to be repurchased (as set forth below), plus interest accrued to the Repurchase Date, as provided herein.

Dated: \_\_\_\_\_

\_\_\_\_\_

Signature

Principal amount to be repurchased (an integral multiple of \$5,500): \_\_\_\_\_

Remaining principal amount following such repurchase (not less than \$5,500): \_\_\_\_\_

NOTICE: The signature to the foregoing Election must correspond to the name as written upon the face of this Security in every particular, without alteration or any change whatsoever.

CONVERSION NOTICE

The undersigned holder of this Security hereby irrevocably exercises the option to convert this Security, or any portion of the principal amount hereof (which is an integral multiple of \$5,500) below designated, into shares of Common Stock in accordance with the terms of this Security, and directs that such shares, together with a check in payment for any fractional share and any Security representing any unconverted principal amount hereof, be delivered to and be registered in the name of the undersigned unless a different name has been indicated below. If shares of Common Stock or Securities are to be registered in the name of a person other than the undersigned, the undersigned will pay

all transfer taxes payable with respect thereto.

Dated: \_\_\_\_\_

\_\_\_\_\_  
Signature

19

If shares or Securities are to be registered in the name of a person other than the holder, please print such person's name and address:

\_\_\_\_\_  
Name

\_\_\_\_\_  
Address

\_\_\_\_\_  
Social Security or other Taxpayer Identification Number, if any

If only a portion of the Securities is to be converted, please indicate:

1. Principal amount to be converted:

\$ \_\_\_\_\_

2. Principal amount and denomination of Security representing unconverted principal amount to be issued:

Amount: \$ \_\_\_\_\_

Denominations: \$ \_\_\_\_\_  
(any integral multiple of \$5,500)

20