

FORM 8-K

CURRENT REPORT

PURSUANT TO SECTION 13 OR 15(D) OF THE  
SECURITIES EXCHANGE ACT OF 1934

JULY 8, 2004

Date of Report (Date of earliest event reported)

DISCOVERY LABORATORIES, INC.  
(Exact name of Registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction  
of incorporation)

000-26422  
(Commission File Number)

94-3171943  
(IRS Employer  
Identification Number)

350 MAIN STREET, SUITE 307  
DOYLESTOWN, PENNSYLVANIA 18901  
(Address of principal executive offices)

(215) 340-4699  
(Registrant's telephone number, including area code)

(Former name or former address, if changed since last report)

ITEM 5. OTHER EVENTS

On July 8, 2004, Discovery Laboratories, Inc. (the "Registrant"), issued a press release to announce the completion of a Committed Equity Financing Facility Arrangement ("CEFF") with Kingsbridge Capital Limited ("Kingsbridge") pursuant to which Kingsbridge has committed to finance up to \$75 million of capital to support the Registrant's future growth. The CEFF is embodied in a Common Stock Purchase Agreement filed herewith as Exhibit 10.1 and a Registration Rights Agreement filed herewith as Exhibit 10.2. Subject to certain limitations, from time to time under the CEFF, the Registrant can require Kingsbridge to purchase newly-issued shares of the Registrant's common stock, par value \$.001 per share (the "Common Stock"), over the course of a 15-trading day period. Subject to limited exceptions, on each trading day of each such financing period, Kingsbridge is required to purchase shares of Common Stock for an aggregate purchase price equal to 1/15 of the applicable financing amount. The Registrant has the right to determine the exact timing, amount and price of any and all financings under the CEFF, subject to certain conditions and limitations. The CEFF allows the Registrant to raise capital as required, at the time, price and in amounts deemed suitable to the Registrant, during the three-year period following the effectiveness of the registration statement to be filed by the Registrant with the Securities and Exchange Commission ("SEC").

In connection with the CEFF, the Registrant issued to Kingsbridge a warrant, a copy of which is filed herewith as Exhibit 4.1, to purchase up to 375,000 shares of Common Stock at an exercise price equal to \$12.0744 per share (the "Warrant"). The Warrant may not be exercised if and to the extent that the shares to be issued to Kingsbridge upon such exercise, when aggregated with other shares of Common Stock beneficially owned, or deemed beneficially owned, by Kingsbridge, would cause Kingsbridge to own more than 9.9% of the outstanding shares of Common Stock on the date of such exercise. The Warrant is exercisable for five years commencing on January 7, 2005. The warrant must be exercised for cash, except in limited circumstances.

Pursuant to the CEFF, the Registrant may access up to and including \$18.75 million per 15-day financing period. The Registrant is not obligated to utilize any of the \$75 million available under the CEFF and there are no minimum

commitment or minimum use penalties. The Registrant may not access the CEFF unless and until the SEC declares effective the registration statement to be filed by the Registrant covering the resale of the shares of Common Stock issuable in connection with the CEFF and the shares of Common Stock underlying the Warrant. Each draw down will be priced over a 15-trading day financing period with the Registrant controlling the minimum acceptable purchase price for any shares to be issued to Kingsbridge during that time. The purchase price for the shares of Common Stock pursuant to the CEFF shall reflect discounts ranging from 6% to 10% of the average market price of the Common Stock during the applicable financing period, with the reduced discounts applying if the price of the Common Stock is equal to \$9.01 or more. However, Kingsbridge shall not be required to purchase any shares of Common Stock on any day of a financing period if and to the extent that such purchase would cause Kingsbridge to purchase a number of shares of Common Stock which, when aggregated with other shares of Common Stock then beneficially owned, or deemed beneficially owned, by Kingsbridge, would result in Kingsbridge owning more than 9.9% of the outstanding shares of Common Stock on such day. There must be at least five trading days between individual financing periods, and individual financing are limited to certain maximum amounts depending on the then current market capitalization of the Registrant.

The CEFF does not contain any restrictions on the Registrant's operating activities, automatic pricing resets or minimum market volume restrictions nor prohibit the Registrant from conducting additional debt or equity financings, including PIPEs, shelf offerings, secondary offerings or any other fixed future-priced securities. Throughout the term of the CEFF, Kingsbridge is restricted from engaging in any transaction intended to reduce its economic risk of owning shares of the Registrant's common stock including, without limitation, the purchase of any option or contract to sell, selling "short" or "short against the box", or otherwise entering into any other security transaction the purpose of which is to hedge its risk of ownership of the Common Stock.

The description of the terms and conditions of the CEFF and the Warrant and the rights and obligations of the Registrant and Kingsbridge in connection therewith are qualified by reference in their entirety to the definitive terms and conditions of the Common Stock Purchase Agreement, the Registration Rights Agreement and the Warrant, forms of which are filed as exhibits to this Report.

#### ITEM 7. FINANCIAL STATEMENTS, PRO FORMA FINANCIAL STATEMENTS AND EXHIBITS

(c) Exhibits:

- 4.1 Class B Investor Warrant
- 10.1 Common Stock Purchase Agreement
- 10.2 Registration Rights Agreement
- 99.1 Press Release dated July 8, 2004

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 hereunto duly authorized.

DISCOVERY LABORATORIES, INC.

By: /s/ Robert J. Capetola

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Name: Robert J. Capetola, Ph.D.  
Title: President and Chief Executive  
Officer

Date: July 8, 2004

Execution Copy

THE WARRANTS REPRESENTED BY THIS CERTIFICATE AND THE SECURITIES ISSUABLE UPON EXERCISE THEREOF HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933 OR THE SECURITIES OR BLUE SKY LAWS OF ANY STATE. NEITHER SUCH WARRANTS NOR SUCH SECURITIES MAY BE SOLD, PLEDGED, HYPOTHECATED OR OTHERWISE TRANSFERRED WITHOUT SUCH REGISTRATION, EXCEPT UPON DELIVERY TO THE COMPANY OF SUCH EVIDENCE AS MAY BE SATISFACTORY TO COUNSEL FOR THE COMPANY TO THE EFFECT THAT ANY SUCH TRANSFER SHALL NOT BE IN VIOLATION OF THE SECURITIES ACT OF 1933 OR APPLICABLE STATE SECURITIES OR BLUE SKY LAWS OR ANY RULE OR REGULATION PROMULGATED THEREUNDER.

DISCOVERY LABORATORIES, INC.

CLASS B INVESTOR WARRANT FOR THE PURCHASE  
OF SHARES OF COMMON STOCK

FOR VALUE RECEIVED, DISCOVERY LABORATORIES, INC., a Delaware corporation (the "COMPANY"), hereby certifies that KINGSBRIDGE CAPITAL LIMITED ("KINGSBRIDGE"), its designees or its permitted assigns is entitled to purchase from the Company, at any time or from time to time commencing on January 7, 2005, and prior to 5:00 P.M., New York City time, on January 6, 2010, up to Three Hundred Seventy-Five Thousand (375,000) fully paid and non-assessable shares of Common Stock (subject to adjustment), \$.001 par value per share, of the Company for \$12.0744 per share (subject to adjustment as provided herein) and an aggregate purchase price equal to \$4,527,900. (Hereinafter, (i) said common stock, \$.001 par value per share, of the Company, is referred to as the "COMMON STOCK," (ii) the shares of Common Stock purchasable hereunder or under any other Warrant (as hereinafter defined) are referred to as the "WARRANT SHARES," (iii) the aggregate purchase price payable for all of the Warrant Shares purchasable hereunder is referred to as the "AGGREGATE WARRANT PRICE," (iv) the price payable for each of the Warrant Shares is referred to as the "PER SHARE WARRANT PRICE," (v) this Warrant and all warrants hereafter issued in exchange or substitution for this warrant or such similar warrants are referred to as the "WARRANTS," and (vi) the holder of this Warrant is referred to as the "HOLDER" and the holder of this Warrant and all other Warrants and Warrant Shares are referred to as the "HOLDERS".

By acceptance of this Warrant, the Holder agrees to comply with all applicable provisions of this Warrant, the Common Stock Purchase Agreement entered into between Kingsbridge and the Company (the "PURCHASE AGREEMENT") and the Registration Rights Agreement entered into between Kingsbridge and the Company (the "REGISTRATION RIGHTS AGREEMENT"), to the same extent as if it were a party thereto.

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1. EXERCISE OF WARRANT. (a) This Warrant may be exercised in whole at any time, or in part from time to time, commencing on January 7, 2005, and prior to 5:00 P.M., New York City time, on January 6, 2010, by the Holder by:

(i) the surrender of this Warrant (with the subscription form at the end hereof duly executed) at the address set forth in Section 9(a) hereof, together with proper payment of the Aggregate Warrant Price, or the proportionate part thereof if this Warrant is exercised in part, with payment for the Warrant Shares made by certified or official bank check payable to the order of the Company; or

(ii) the surrender of this Warrant (with the cashless exercise form at the end hereof duly executed) (a "CASHLESS EXERCISE") at the address set forth in Section 10(a) hereof; provided, that a Cashless Exercise may only be effected by the Holder and the Company during an Ineffective Period or a Blackout Period (as such terms are defined in the Registration Rights Agreement) and where the Holder may not sell all the Warrant Shares to be issued in connection with such Cashless Exercise in a single transaction pursuant to Rule 144 promulgated under the Securities Act of 1934 as of the date of such Cashless Exercise. In the event of a Cashless Exercise in accordance with this Section 1(a), Holder shall exchange this Warrant for that number of Warrant Shares subject to such Cashless Exercise multiplied by a fraction, the numerator of which shall be the difference between (A) the "Current Market Price," which is defined as the closing sale price of the Common Stock on the Trading Day (as defined in the Purchase Agreement) prior to the date of such surrender or, in case no such reported sales take place on such Trading Day, the average of the last reported bid and asked prices of the Common Stock on such Trading Day, in either case on the principal national securities exchange on which the Common Stock is admitted to trading or listed, or if not listed or admitted to trading on any such exchange, the representative closing sale price of the Common Stock

as reported by Nasdaq, or other similar organization if Nasdaq is no longer reporting such information, or, if the Common Stock is not reported on Nasdaq, the high per share sale price for the Common Stock in the over-the-counter market as reported by the National Quotation Bureau or similar organization, or if not so available, the fair market value of the Common Stock as determined in good faith by the Board of Directors of the Company (the "BOARD") and (B) the Per Share Exercise Price, and the denominator of which shall be the Current Market Price. For purposes of any computation under this Section 1(a), the Current Market Price shall be based on the Trading Day immediately prior to the Cashless Exercise. The "Closing Sales Price" shall be the reported per share closing sales price, regular way, of the Common Stock on the Nasdaq SmallCap Market (or on the Nasdaq National Market or a national securities exchange, as the case may be) at 4:00 PM New York Time on the applicable Trading Day. If, at any time after July 7, 2006, a registration statement on Form S-1 under the Securities Act of 1933 (the "ACT") or such other form as deemed appropriate by counsel to the Company for the registration for the resale by the Holder of (x) the shares of Common Stock of the Company that may be purchased under the Purchase Agreement, (y) the Warrant Shares or (z) any securities issued or issuable with respect to any of the foregoing by way of exchange, stock dividend or stock split or in connection with a combination of shares, recapitalization, merger, consolidation or other reorganization or otherwise, has been declared effective by the Commission and remains effective, the Company may permit or require the Holder to effect a Cashless Exercise in connection with the exercise of this Warrant.

(b) If this Warrant is exercised in part, this Warrant must be exercised for a number of whole shares of Common Stock and the Holder is entitled to receive a new Warrant covering the Warrant Shares that have not been exercised and setting forth the proportionate part of the Aggregate Warrant Price applicable to such Warrant Shares.

(c) Upon surrender of this Warrant, the Company will (i) issue a certificate or certificates in the name of the Holder, or its nominee, for the largest number of whole shares of the Common Stock to which the Holder shall be entitled and, if this Warrant is exercised in whole, in lieu of any fractional share of Common Stock to which the Holder shall be entitled, pay to the Holder cash in an amount equal to the fair value of such fractional share (determined in such reasonable manner as the Board shall determine) and (ii) deliver the other securities and properties receivable upon the exercise of this Warrant, or the proportionate part thereof if this Warrant is exercised in part, pursuant to the provisions of this Warrant.

(d) The Holder may not exercise this Warrant such that the number of Warrant Shares to be received pursuant to such exercise aggregated with all other shares of Common Stock then owned by the Holder beneficially or deemed beneficially owned by the Holder would result in the Holder owning more than 9.9% of all of such Common Stock as would be outstanding on such Exercise Date, as determined in accordance with Section 13(d) of the Exchange Act of 1934 and the rules and regulations promulgated thereunder.

2. RESERVATION OF WARRANT SHARES; LISTING. The Company agrees and covenants that, prior to the expiration of this Warrant, the Company shall at all times (i) have authorized and in reserve, and shall keep available, solely for issuance and delivery upon the exercise of this Warrant, the shares of Common Stock and other securities and properties receivable upon the exercise of this Warrant and shall be validly issued and non-assessable, free and clear of all restrictions on sale or transfer, other than under Federal or state securities or blue sky laws, and free and clear of all preemptive rights and rights of first refusal and (ii) use its best efforts to keep the Warrant Shares authorized for listing on the Nasdaq National Market, the SmallCap Market or any national securities exchange on which the Common Stock is traded.

3. PROTECTION AGAINST DILUTION. (a) If the Company, at any time while this Warrant is unexpired and not exercised in full, (i) reclassifies or changes its Common Stock (other than a change in par value or as a result of a subdivision or combination of Common Stock issuable upon exercise of the Warrant) or (ii) consolidates, merges or effects a mandatory share exchange with or into another corporation (other than a merger or mandatory share exchange with another corporation in which the Company is a continuing corporation and that does not result in any reclassification or change, other than a change in par value or as a result of a subdivision or combination of Common Stock issuable upon exercise of the Warrant) at any time while this Warrant is unexpired and not exercised in full, then in any such event the Company, or such successor or purchasing corporation, as the case may be, shall, without payment of any additional consideration therefore, amend this Warrant or issue a new Warrant providing that the Holder shall have rights not less favorable to the Holder than those then applicable to this Warrant and to receive upon exercise under such

amendment of this Warrant or new Warrant, in lieu of each share of Common Stock theretofore issuable upon exercise of the Warrant hereunder, the kind and amount of shares of stock, other securities, money or property receivable upon such reclassification, change, consolidation, merger or mandatory share exchange by the holder of one share of Common Stock issuable upon exercise of the Warrant had the Warrant been exercised immediately prior to such reclassification, change, consolidation, merger or mandatory share exchange. Such amended Warrant shall provide for adjustments which shall be as nearly equivalent as may be practicable to the adjustments provided for in this Section 3. The provisions of this Section 3(a) shall similarly apply to successive reclassifications, changes, consolidations, mergers, mandatory share exchanges and sales and transfers.

(b) If the Company, at any time while this Warrant is unexpired and not exercised in full, shall subdivide its Common Stock, the Per Share Warrant Price shall be proportionately reduced as of the effective date of such subdivision, or, if the Company shall take a record of holders of its Common Stock for the purpose of so subdividing, as of such record date, whichever is earlier. If the Company, at any time while this Warrant is unexpired and not exercised in full, shall combine its Common Stock, the Per Share Warrant Price shall be proportionately increased as of the effective date of such combination, or, if the Company shall take a record of holders of its Common Stock for the purpose of so combining, as of such record date, whichever is earlier.

(c) If the Company, at any time while this Warrant is unexpired and not exercised in full, shall pay a dividend or make a distribution on the outstanding shares of Common Stock in shares of its Common Stock, then, as of the effective date of payment of such dividend or distribution, the number and kind of shares of Common Stock receivable upon exercise of this Warrant shall be proportionately adjusted so that the Holder shall thereafter be entitled to receive the aggregate number of shares of Common Stock which, if such Warrant had been exercised immediately prior to such time, it would have owned upon such exercise and been entitled to receive by virtue of such dividend or distribution. The provisions of this Section 3(c) shall not apply under any of the circumstances for which an adjustment is provided in Sections 3(a) or 3(b).

(d) No adjustment in the Per Share Warrant Price shall be required unless such adjustment would require an increase or decrease of at least \$0.05 per share of Common Stock; provided, however, that any adjustments which by reason of this Section 3(d) are not required to be made shall be carried forward and taken into account in any subsequent adjustment; provided, further, however, the Company shall be entitled to make such reductions in the Per Share Warrant Price, in addition to those required by this Section 3, as it in its discretion shall deem to be advisable in order that any stock dividend, subdivision of shares or distribution of rights to purchase stock or securities convertible or exchangeable for stock hereafter made by the Company to its stockholders shall not be taxable. All calculations under this Section 3 shall be made to the nearest cent or to the nearest 1/100th of a share, as the case may be.

(e) Upon the expiration of any rights, options, warrants or conversion privileges with respect to the issuance of which an adjustment to the Per Share Warrant Price had been made, if such shall not have been exercised, the number of Warrant Shares purchasable upon exercise of this Warrant, to the extent this Warrant has not then been exercised, shall, upon such expiration, be readjusted and shall thereafter be such as they would have been had they been originally adjusted (or had the original adjustment not been required, as the case may be)



on the basis of (A) the fact that Common Stock, if any, actually issued or sold upon the exercise of such rights, options, warrants or conversion privileges and (B) the fact that such shares of Common Stock, if any, were issued or sold for the consideration actually received by the Company upon such exercise plus the consideration, if any, actually received by the Company for the issuance, sale or grant of all such rights, options, warrants or conversion privileges whether or not exercised; provided, however, that no such readjustment shall have the effect of decreasing the number of Warrant Shares purchasable upon exercise of this Warrant by an amount in excess of the amount of the adjustment initially made in respect of the issuance, sale or grant of such rights, options, warrants or conversion privileges.

4. FULLY PAID STOCK; TAXES. The Warrant Shares delivered upon the exercise of this Warrant shall at the time of such delivery, be duly authorized, validly issued and outstanding, fully paid and non-assessable, and not subject to preemptive rights or rights of first refusal, and the Company will take all such actions as may be necessary to assure that the par value, if any, per Warrant Share is at all times equal to or less than the then Per Share Warrant Price. The Company shall pay all documentary, stamp or similar taxes and other similar governmental charges that may be imposed with respect to the issuance or delivery of any Warrant Shares (other than income taxes); provided, however, that if the Warrant Shares are to be delivered in a name other than the name of the Holder, no such delivery shall be made unless the person requesting the same has paid to the Company the amount of transfer taxes or charges incident thereto, if any.

5. INVESTMENT INTENT; LIMITED TRANSFERABILITY. (a) The Holder represents, by accepting this Warrant, that it understands that this Warrant and any securities obtainable upon exercise of this Warrant have not been registered for sale under Federal or state securities or blue sky laws and are being offered and sold to the Holder pursuant to one or more exemptions from the registration requirements of such securities laws. In the absence of an effective registration of such securities or an exemption therefrom, any certificates for such securities shall bear a legend substantially similar to the legend set forth on the first page of this Warrant. The Holder understands that it must bear the economic risk of its investment in this Warrant and any securities obtainable upon exercise of this Warrant for an indefinite period of time, as this Warrant and such securities have not been registered under Federal or state securities or blue sky laws and therefore cannot be sold unless subsequently registered under such laws, unless an exemption from such registration is available.

(b) The Holder agrees and acknowledges that this Warrant, or any portion thereof, and any such securities will not be sold or otherwise transferred unless (i) a registration statement with respect to such transfer is effective under the Act and any applicable state securities or blue sky laws or (ii) such sale or transfer is made pursuant to one or more exemptions from the Act.

(c) The Holder agrees and acknowledges that in addition to the limitations set forth in the Registration Rights Agreement with respect to Registrable Securities, this Warrant may not be sold, transferred, assigned or hypothecated by the Holder except in compliance with the provisions of the Act and the applicable state securities or blue sky laws, and is so transferable only upon the books of the Company which it shall cause to be maintained for such purpose. The Company may treat the registered Holder of this Warrant as it appears on the Company's books at any time as the Holder for all purposes. The Company shall

permit any Holder of a Warrant or its duly authorized attorney, upon written request during ordinary business hours, to inspect and copy or make extracts from its books showing the registered holders of Warrants. All Warrants issued upon the transfer or assignment of this Warrant will be dated the same date as this Warrant, and all rights of the holder thereof shall be identical to those of the Holder.

(d) The Holder represents that it has been afforded (i) the opportunity to ask such questions as it has deemed necessary of, and to receive answers from, representatives of the Company concerning the terms and conditions of the Warrants or the exercise of the Warrants and the finance operations and business of the Company and (ii) the opportunity to request such additional information which the Company possesses or can acquire without unreasonable effort or expense. Nothing contained in this Section 5(d) shall alter, amend or change Holder's reliance on the representations, covenants or warranties contained herein.

(e) The Holder represents that it did not (i) receive or review any advertisement, article, notice or other communication published in a newspaper or magazine or similar media or broadcast over television or radio, whether closed circuit, or generally available; or (ii) attend any seminar, meeting or investor or other conference whose attendees were, to such Holder's knowledge, invited by any general solicitation or general advertising.

(f) The Holder represents that it is an "accredited investor" within the meaning of Regulation D promulgated under the Act. Such Holder is acquiring the Warrants for its own account and not with a present view to, or for sale in connection with, any distribution thereof in violation of the registration requirements of the Act, without prejudice, however, to such Holder's right, subject to the provisions of the Purchase Agreement, the Registration Rights Agreement and this Warrant, at all times to sell or otherwise dispose of all or any part of the Warrants and Warrant Shares.

(g) The Holder represents that it, either by reason of the Holder's business or financial experience or the business or financial experience of its professional advisors (who are unaffiliated with and who are not compensated by the Company or any affiliate, finder or selling agent of the Company, directly or indirectly), has such sophistication, knowledge and experience in financial and business matters as to be capable of evaluating the merits and risks of its investment in the Company and the capacity to protect the Holder's interests in connection with the transactions contemplated by this Warrant, the Purchase Agreement and the Registration Rights Agreement.

(h) The Holder represents that it has the ability to bear the economic risks of its investment for an indefinite period of time and could afford a complete loss of its investment.

(i) The Holder agrees and acknowledges that the representations made by the Holder in this Section 5 are conditions to the exercise of the Warrant.

(j) Nothing in this Section 5 shall affect in any way the Holder's obligations under any agreement to comply with all applicable securities laws upon resale of the Warrant Shares.

6. LOSS, ETC., OF WARRANT. Upon receipt of evidence satisfactory to the Company of the loss, theft, destruction or mutilation of this Warrant, and of indemnity reasonably satisfactory to the Company, if lost, stolen or destroyed, and upon surrender and cancellation of this Warrant, if mutilated, the Company shall execute and deliver to the Holder a new Warrant of like date, tenor and denomination.

7. HOLDER NOT STOCKHOLDER. This Warrant does not confer upon the Holder any right to vote on or consent to or receive notice as a stockholder of the Company, as such, in respect of any matters whatsoever, nor any other rights or liabilities as a stockholder, prior to the exercise hereof; this Warrant does, however, require certain notices to Holders as set forth herein.

8. NOTICES OF RECORD DATE, ETC. If the Company shall propose at any time to effect or to establish (i) a record date for the holders of the Common Stock for the purpose of entitling them to receive any dividend or other distribution, or any right to subscribe for, purchase or otherwise acquire any shares or stock of any class or any other securities or to receive any other right or (ii) any voluntary or involuntary dissolution, liquidation or dissolution of the Company, then notice of any such proposed action shall be mailed to the Holders not less than 10 days prior to such event.

9. NOTICES. All notices, demands, requests, consents, approvals, and other communications required or permitted hereunder shall be in writing and, unless otherwise specified herein, shall be (i) personally served, (ii) deposited in the mail, registered or certified, return receipt requested, postage prepaid, (iii) delivered by reputable air courier service with charges prepaid or (iv) transmitted by hand delivery, telegram or facsimile, addressed as set forth below or to such other address as such party shall have specified most recently by written notice given in accordance herewith. Any notice or other communication required or permitted to be given hereunder shall be deemed effective (a) upon hand delivery or delivery by facsimile, with accurate confirmation generated by the transmitting facsimile machine, at the address or number designated below (if delivered on a business day during normal business hours where such notice is to be received), or the first business day following such delivery (if delivered other than on a business day during normal business hours where such notice is to be received) or (b) on the second business day following the date of mailing by express courier service, fully prepaid, addressed to such address, or upon actual receipt of such mailing, whichever shall first occur. The addresses for such communications shall be:

If to the Company:

Discovery Laboratories, Inc.  
350 South Main Street  
Suite 307  
Doylestown, Pennsylvania 18901  
Telephone: (215) 340-4699  
Facsimile: (215) 340-3940  
Attention: Chief Financial Officer and General Counsel

with a copy (which shall not constitute notice) to:

Dickstein Shapiro Morin & Oshinsky LLP  
1177 Avenue of the Americas, 41st Floor  
New York, NY 10036-2714  
Telephone: (212) 835-1400  
Facsimile: (212) 997-9880  
Attention: Ira L. Kotel

if to the Holder, at such address as the Holder has designated in writing to the Company.

10. ASSIGNMENT. Assuming the conditions of Sections 5(b) and 5(c) have been satisfied, the Holder may sell, transfer, assign, pledge or otherwise dispose of this Warrant (each of the foregoing, a "Transfer"), in whole or in part, but only to an Affiliate of the Holder. The Holder shall deliver a written notice to Company, substantially in the form of the Assignment attached hereto, indicating the person or persons to whom the Warrant shall be Transferred and the respective number of warrants to be Transferred to each assignee. The Company shall effect the Transfer within 10 days, and shall deliver to the Transferee(s) designated by the Holder a Warrant or Warrants of like tenor and terms for the appropriate number of shares. In connection with and as a condition of any such proposed Transfer, the Company may request the Holder to provide an opinion of counsel to the Holder in form and substance reasonably satisfactory to the Company to the effect that the proposed Transfer complies with all applicable federal and state securities laws.

11. HEADINGS. The headings of this Warrant have been inserted as a matter of convenience and shall not affect the construction hereof.

12. APPLICABLE LAW. This Warrant shall be governed by and construed in accordance with the laws of the State of New York without giving effect to the principles of conflicts of law thereof.

13. AMENDMENT, WAIVER, ETC. Except as expressly provided herein, neither this Warrant nor any term hereof may be amended, waived, discharged or terminated other than by a written instrument signed by the party against whom enforcement of any such amendment, waiver, discharge or termination is sought.

IN WITNESS WHEREOF, the Company has caused this Warrant to be executed this 7th day of July, 2004.

DISCOVERY LABORATORIES, INC.

By: /s/ John G. Cooper

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Name: John G. Cooper  
Title: Executive Vice President and  
Chief Financial Officer

SUBSCRIPTION

The undersigned, \_\_\_\_\_, pursuant to the provisions of the foregoing Warrant, hereby elects to exercise such Warrant by agreeing to subscribe for and purchase \_\_\_\_\_ shares (the "Warrant Shares") of Common Stock, par value \$.001 per share, of Discovery Laboratories, Inc. (the "Company"), and hereby makes payment of \$\_\_\_\_\_ by certified or official bank check in payment of the exercise price therefor.

As a condition to this subscription, the undersigned hereby represents and warrants to the Company that the representations and warranties of Section 5 of the Warrant are true and correct as of the date hereof as if they had been made on such date with respect to the Warrant Shares. The undersigned further acknowledges that the sale, transfer, assignment or hypothecation of the Warrant Shares to be issued upon exercise of this Warrant is subject to the terms and conditions contained in Sections 1 and 5 of this Warrant.

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

Address: \_\_\_\_\_  
\_\_\_\_\_

CASHLESS EXERCISE

The undersigned, \_\_\_\_\_, pursuant to the provisions of the foregoing Warrant, hereby elects to exercise such Warrant by agreeing to subscribe for and purchase \_\_\_\_\_ shares (the "Warrant Shares") of Common Stock, par value \$.001 per share, of Discovery Laboratories, Inc. (the "Company"), pursuant to the Cashless Exercise provisions of the Warrant.

As a condition to this subscription, the undersigned hereby represents and warrants to the Company that the representations and warranties of Section 5 of the Warrant are true and correct as of the date hereof as if they had been made on such date with respect to the Warrant Shares. The undersigned further acknowledges that the sale, transfer, assignment or hypothecation of the Warrant Shares to be issued upon exercise of this Warrant is subject to the terms and conditions contained in Sections 1 and 5 of this Warrant.

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

Address: \_\_\_\_\_  
\_\_\_\_\_

ASSIGNMENT

FOR VALUE RECEIVED \_\_\_\_\_ hereby sells, assigns and transfers unto \_\_\_\_\_ the foregoing Warrant and all rights evidenced thereby, and does irrevocably constitute and appoint \_\_\_\_\_, attorney, to transfer said Warrant on the books of Discovery Laboratories, Inc. (the "Company"). As a condition to this assignment, the Holder acknowledges that its assignee must deliver a written instrument to the Company that the representations and warranties of Section 5 of the Warrant are true and correct as of the date hereof as if they had been made by such assignee on such date with respect to the Warrants.

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

Address: \_\_\_\_\_  
\_\_\_\_\_

PARTIAL ASSIGNMENT

FOR VALUE RECEIVED \_\_\_\_\_ hereby assigns and transfers unto \_\_\_\_\_ the right to purchase \_\_\_\_\_ shares of the Common Stock, par value \$.001 per share, of Discovery Laboratories, Inc. (the "Company"), as set forth in the foregoing Warrant, and a proportionate part of said Warrant and the rights evidenced thereby, and does irrevocably constitute and appoint \_\_\_\_\_, attorney, to transfer that part of said Warrant on the books of the Company. As a condition to this assignment, the Holder acknowledges that its assignee must deliver a written instrument to the Company that the representations and warranties of Section 5 of the Warrant are true and correct as of the date hereof as if they had been made by such assignee on such date with respect to the Warrants.

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

Address: \_\_\_\_\_  
\_\_\_\_\_

COMMON STOCK PURCHASE AGREEMENT

BY AND BETWEEN

KINGSBRIDGE CAPITAL LIMITED

AND

DISCOVERY LABORATORIES, INC.

DATED AS OF JULY 7, 2004

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This COMMON STOCK PURCHASE AGREEMENT is entered into as of the 7th day of July, 2004 (this "Agreement"), by and between Kingsbridge Capital Limited, an entity organized and existing under the laws of the British Virgin Islands (the "Investor"), and DISCOVERY LABORATORIES, INC., a corporation organized and existing under the laws of the State of Delaware (the "Company").

WHEREAS, the parties desire that, upon the terms and subject to the conditions and limitations set forth herein, the Company may issue and sell to the Investor, from time to time, and the Investor shall purchase from the Company, up to \$75 million of shares of Common Stock (as defined below); and

WHEREAS, such investments will be made in reliance upon the provisions of Section 4(2) ("Section 4(2)") and Regulation D ("Regulation D") of the United States Securities Act of 1933 and the rules and regulations promulgated thereunder (the "Securities Act"), and/or upon such other exemptions from the registration requirements of the Securities Act as may be available with respect to any or all of the investments in Common Stock to be made hereunder; and

WHEREAS, the parties hereto are concurrently entering into a Registration Rights Agreement in the form of Exhibit A hereto (the "Registration Rights Agreement") pursuant to which the Company intends to register the Common Stock issued and sold to the Investor under this Agreement and under the Warrant (as defined below), upon the terms and subject to the conditions and limitations set forth therein; and

WHEREAS, in consideration for the Investor's execution and delivery of, and its performance of its obligations under, this Agreement, the Company is concurrently issuing to the Investor a Warrant in the form of Exhibit B hereto (the "Warrant") pursuant to which the Investor may purchase from the Company up to 375,000 shares of Common Stock, upon the terms and subject to the conditions set forth therein;

NOW, THEREFORE, the parties hereto agree as follows:

## ARTICLE I

### DEFINITIONS

Section 1.01. "Affiliate" shall mean, as to the party specified, any Person which directly or indirectly Controls, is Controlled by or is under common Control with, such party.

Section 1.02. "Blackout Amount" shall have the meaning assigned to such term in the Registration Rights Agreement.

Section 1.03. "Bloomberg" means the interactive financial information network operated by Bloomberg L.P.

Section 1.04. "Charter" shall have the meaning assigned to such term in Section 4.03 hereof.

Section 1.05. "Closing Date" means the date on which this Agreement is executed and delivered by the Company and the Investor.

Section 1.06. "Commission" means the United States Securities and Exchange Commission.

Section 1.07. "Commission Documents" shall have the meaning assigned to such term in Section 4.06 hereof.

Section 1.08. "Commitment Period" means the period commencing on the Effective Date and expiring on the earliest to occur of (x) the date on which the Investor shall have purchased Shares pursuant to this Agreement for an aggregate purchase price equal to the Maximum Commitment Amount, (y) the date this Agreement is terminated pursuant to Article IX hereof and (z) the date occurring 36 months from the Effective Date.

Section 1.09. "Common Stock" means the common stock of the Company, par value \$0.001 per share.

Section 1.10. "Control" (including the terms "Controlling," "Controlled by" and "under common Control with") means the possession, direct or indirect, of the power, either individually or with others, to direct or cause the direction of the management and policies of a Person, whether through the ownership of voting securities, by contract, or otherwise as set forth in Rule 405 promulgated under the Securities Act.

Section 1.11. "Condition Satisfaction Date" shall have the meaning assigned to such term in Article VII hereof.

Section 1.12. "Damages" means any loss, claim, damage, liability, cost and expense (including, without limitation, reasonable attorneys' fees and expenses and reasonable costs and expenses of expert witnesses and investigation).

Section 1.13. "Draw Down" shall have the meaning assigned to such term in Section 3.01 hereof.

Section 1.14. "Draw Down Amount" means the actual amount of a Draw Down paid to the Company.

Section 1.15. "Draw Down Discount Price" means (i) 90% of the VWAP on any Trading Day during the Draw Down Pricing Period when the VWAP equals to or exceeds \$5.00 but is less than or equal to \$9.00, (ii) 92% of the VWAP on any Trading Day during the Draw Down Pricing Period when the VWAP exceeds \$9.00 but is less than or equal to \$14.00 and (iii) 94% of the VWAP on any Trading Day during the Draw Down Pricing Period when the VWAP exceeds \$14.00.

Section 1.16. "Draw Down Notice" shall have the meaning assigned to such term in Section 3.01 hereof.

Section 1.17. "Draw Down Pricing Period" shall mean, with respect to each Draw Down, a period of fifteen (15) consecutive Trading Days beginning on the first Trading Day specified in a Draw Down Notice.

Section 1.18. "Effective Date" means the first Trading Day immediately following the date on which the Registration Statement is declared effective by the Commission.

Section 1.19. "Exchange Act" means the federal Securities Exchange Act of 1934, as amended, and the rules and regulations promulgated thereunder.

Section 1.20. "Knowledge" means the actual knowledge of the Company's Chief Executive Officer, Chief Financial Officer or any Senior or Executive Vice President.

Section 1.21. "Legend" shall have the meaning specified in Section 8.1.

Section 1.22. "Make Whole Amount" shall have the meaning specified in Section 3.10.

Section 1.23. "Market Capitalization" means, as of any Trading Day, the product of (i) the closing sale price of the Common Stock as reported by Bloomberg using the AQR function and (ii) the number of outstanding shares of Common Stock of the Company as reported by Bloomberg using the DES function.

Section 1.24. "Material Adverse Effect" means any effect on the business, operations, properties or financial condition of the Company and its consolidated subsidiaries that is material and adverse to the Company and such subsidiaries, taken as a whole, and/or any condition, circumstance or situation that would prohibit or otherwise interfere with the ability of the Company to perform any of its obligations under this Agreement, the Registration Rights Agreement or the Warrant in any material respect; provided, that none of the following shall constitute a "Material Adverse Effect": (i) the effects of conditions or events that are generally applicable to the capital, financial, banking, currency, biotechnology or pharmaceutical markets; (ii) any changes or effects resulting from the announcement or consummation of the transactions contemplated by this Agreement, including, without limitation, any changes or effects associated with any particular Draw Down; and (iii) changes in the market price of the Common Stock.

Section 1.25. "Maximum Commitment Amount" means \$75 million in aggregate Draw Down Amounts.

Section 1.26. "Maximum Draw Down Amount" means 4.9% of the Company's Market Capitalization at the time of the Draw Down; provided, however, that such amount shall not exceed \$18.75 million in respect of any Draw Down.

Section 1.27. "NASD" means the National Association of Securities Dealers, Inc.

Section 1.28. "Other Financing" shall have the meaning assigned to such term in Section 6.07 hereof.

Section 1.29. "Permitted Transaction" shall have the meaning assigned to such term in Section 6.07 hereof.

Section 1.30. "Person" means any individual, corporation, partnership, limited liability company, association, trust or other entity or organization, including any government or political subdivision or an agency or instrumentality thereof.

Section 1.31. "Principal Market" means the National Market or the SmallCap Market of the National Association of Securities Dealers, Inc. Automated Quotation Service, the American Stock Exchange or the New York Stock Exchange, whichever is at the time the principal trading exchange or market for the Common Stock.

Section 1.32. "Prohibited Transaction" shall have the meaning assigned to such term in Section 6.08 hereof.

Section 1.33. "Prospectus" as used in this Agreement means the prospectus in the form included in the Registration Statement, as supplemented from time to time.

Section 1.34. "Registrable Securities" means (i) the Shares, (ii) the Warrant Shares and (iii) any securities issued or issuable with respect to any of the Shares or Warrant Shares by way of exchange, stock dividend or stock split or in connection with a combination of shares, recapitalization, merger, consolidation or other reorganization or otherwise. As to any particular Registrable Securities, once issued, such securities shall cease to be Registrable Securities when (w) the Registration Statement has been declared effective by the Commission and such Registrable Securities have been disposed of pursuant to the Registration Statement, (x) such Registrable Securities may be sold under the applicable conditions of Rule 144 (or any similar provision then in force) promulgated under the Securities Act ("Rule 144"), (y) such time as such Registrable Securities have been otherwise transferred to holders who may trade such shares without restriction under the Securities Act, and the Company has delivered a new certificate or other evidence of ownership for such securities not bearing a restrictive legend or (z) in the opinion of counsel to the Company (which may be internal counsel), such Registrable Securities may be sold without registration and without any time, volume or manner limitations pursuant to Rule 144(k) (or any similar provision then in effect) under the Securities Act.

Section 1.35. "Registration Rights Agreement" shall have the meaning set forth in the recitals of this Agreement.

Section 1.36. "Registration Statement" shall have the meaning assigned to such term in the Registration Rights Agreement.

Section 1.37. "Regulation D" shall have the meaning set forth in the recitals of this Agreement.

Section 1.38. "Section 4(2)" shall have the meaning set forth in the recitals of this Agreement.



Section 1.39. "Securities Act" shall have the meaning set forth in the recitals of this Agreement.

Section 1.40. "Settlement Date" shall have the meaning assigned to such term in Section 3.06 hereof.

Section 1.41. "Shares" means the shares of Common Stock that are and/or may be purchased hereunder.

Section 1.42. "Threshold Price" means the lowest "Draw Down Discount Price" (as specified by the Company in a Draw Down Notice) at which the Company will agree to sell Shares during the applicable Draw Down Pricing Period, which price shall not be less than \$5.00 per share.

Section 1.43. "Trading Day" means any day other than a Saturday or a Sunday on which the Principal Market is open for trading in equity securities.

Section 1.44. "Underwriter" shall mean any underwriter (other than the Investor, to the extent it is deemed to be a statutory underwriter) participating in any disposition of the Registrable Securities on behalf of the Investor pursuant to the Registration Statement.

Section 1.45. "VWAP" means the volume weighted average price per share (the aggregate sales price of all trades of Common Stock during each Trading Day divided by the total number of shares of Common Stock traded during such Trading Day) of the Common Stock during any Trading Day as reported by Bloomberg using the AQR function.

Section 1.46. "Warrant" shall have the meaning set forth in the recitals of this Agreement.

Section 1.47. "Warrant Shares" means the shares of Common Stock issuable to the Investor upon exercise of the Warrant.

## ARTICLE II

### PURCHASE AND SALE OF COMMON STOCK

Section 2.01. Purchase and Sale of Stock. Upon the terms and subject to the conditions and limitations set forth in this Agreement, the Company shall issue and sell to the Investor, and the Investor shall purchase from the Company, a number of shares of Common Stock with an aggregate purchase price (in Draw Down Amounts) equal to up to the Maximum Commitment Amount, consisting of Draw Downs in accordance with Article III hereof.

Section 2.02. Closing. In consideration of, subject to and in express reliance upon the representations, warranties, covenants, terms and conditions of this Agreement, the Company agrees to issue and sell to the Investor, and the Investor agrees to purchase from the Company, that number of the Shares to be issued in connection with each Draw Down. The closing of the execution and delivery of this Agreement (the "Closing") shall take place at the offices of Clifford Chance US LLP, 31 West 52nd Street, New York, NY 10019 at 2:00 p.m. local time on July 7, 2004, or at such other time and place or on such date as the Investor and the Company may agree upon (the "Closing Date"). Each party shall deliver all documents, instruments and writings required to be delivered by such party pursuant to this Agreement at or prior to the Closing.

Section 2.03. Warrant. On the Closing Date, the Company shall issue and deliver the Warrant to the Investor.

### ARTICLE III

#### DRAW DOWN TERMS

Subject to the satisfaction of the conditions hereinafter set forth in this Agreement, the parties agree as follows:

Section 3.01. Draw Down Notice. The Company, may, in its sole discretion, issue one or more Draw Down Notices with respect to Draw Downs (each, a "Draw Down") during the Commitment Period, which Draw Downs the Investor will be obligated to accept. The Company shall inform the Investor via facsimile transmission in accordance with Section 12.04, with a copy to the Investor's counsel, as to the Draw Down Amount the Company wishes to exercise before commencement of trading on the first Trading Day of any Draw Down Pricing Period (the "Draw Down Notice"). In addition to the Draw Down Amount, each Draw Down Notice shall specify the Threshold Price in respect of the applicable Draw Down and shall designate the first Trading Day of the Draw Down Pricing Period. In no event shall any Draw Down Amount exceed the Maximum Draw Down Amount. Each Draw Down Notice shall be accompanied by a certificate, signed by the Chief Executive Officer or Chief Financial Officer dated as of the date of such Draw Down Notice, in the form of Exhibit C hereof.

Section 3.02. Number of Shares. The number of Shares to be issued in connection with each Draw Down shall be equal to the sum of one fifteenth (1/15th) of such Draw Down Amount divided by the applicable Draw Down Discount Price for each Trading Day of the Draw Down Pricing Period for which the Draw Down Discount Price equals or exceeds the Threshold Price.

Section 3.03. Limitation on Draw Downs. Only one Draw Down shall be permitted for each Draw Down Pricing Period.

Section 3.04. Trading Cushion. Unless the parties agree otherwise in writing, there shall be a minimum of five (5) Trading Days between the expiration of any Draw Down Pricing Period and the beginning of the next succeeding Draw Down Pricing Period.

Section 3.05. Expiration of Draw Downs. Each Draw Down will expire on the last Trading Day of each Draw Down Pricing Period.

Section 3.06. Settlement. The number of Shares purchased by the Investor with respect to each Draw Down shall be determined and settled on a periodic basis in respect of the applicable Draw Down Pricing Period. Settlement in respect of each determination shall be made at the Company's sole discretion, but in any event, not later than the third Trading Day after the fifth, tenth and fifteenth Trading Day of the Draw Down Pricing Period. Each date on which settlement of the purchase and sale of Shares occurs hereunder being referred to as a "Settlement Date." The Investor shall provide the Company with delivery instructions for the Shares to be issued at each Settlement Date at least two (2) Trading Days in advance of such Settlement Date (except to the extent previously provided). The number of Shares actually issued shall be rounded to the nearest whole number of Shares.

Section 3.07. Delivery of Shares; Payment of Draw Down Amount. On each Settlement Date, the Company shall deliver the Shares purchased by the Investor to the Investor or its designees via book-entry through the Depository Trust Company to an account designated by the Investor in accordance with Section 3.06 upon receipt of payment therefor from the Investor to the Company's designated account by wire transfer of immediately available funds.

Section 3.08. Threshold Price. For each Trading Day during a Draw Down Pricing Period that the Draw Down Discount Price is less than the Threshold Price, no Shares shall be purchased or sold in respect of such Trading Day, the total amount of the Draw Down Amount in respect of such Draw Down Pricing Period shall be reduced by one fifteenth (1/15th) and the amount of the Draw Down Amount not so purchased or sold shall continue to be available in future Draw Downs and as part of the Maximum Commitment Amount. If trading in the Common Stock is suspended for any reason for more than three (3) consecutive or non-consecutive hours during any Trading Day during a Draw Down Pricing Period, the Draw Down Discount Price shall be deemed to be less than the Threshold Price for that Trading Day.

Section 3.09. Other Issuances. If during any Draw Down Pricing Period, the Company shall issue any shares of Common Stock in connection with a Prohibited Transaction without the prior written consent of the Investor, then the applicable Draw Down Notice shall be deemed null and void and the Investor shall promptly return to the Company any and all Shares transferred to the Investor in respect of any Settlement Date(s) during such Draw Down Pricing Period and the Company shall promptly thereafter pay to the Investor by wire transfer of immediately available funds to an account designated by the Investor that portion of the applicable Draw Down Amount paid to the Company in respect of such Settlement Date(s).

Section 3.10. Failure to Deliver Shares. If on any Settlement Date, the Company fails to deliver the Shares to be purchased by the Investor, and such failure is not cured within ten (10) Trading Days following the date on which the Investor delivered payment for such Shares, the Company shall pay to the Investor on demand in cash by wire transfer of immediately available funds to an account designated by the Investor the "Make Whole Amount;" provided, however, that in the event that the Company is prevented from delivering Shares in respect of any such Settlement Date in a timely manner by any fact or circumstance that is reasonably within the control of, or directly attributable to, the Investor, then such ten (10) Trading Day period shall be automatically extended until such time as such fact or circumstance is cured. As used herein, the Make Whole Amount shall be an amount equal to the sum of (i) the Draw Down Amount actually paid by the Investor in respect of such Shares plus (ii) an amount equal to the actual loss suffered by the Investor in respect of sales to subsequent purchasers, pursuant to transactions entered into before the Settlement Date, of the Shares that were required to be delivered by the Company, which shall be based upon documentation reasonably satisfactory to the Company demonstrating the difference (if greater than zero) between (A) the price per share paid by the Investor to purchase such number of shares of Common Stock necessary for the Investor to meet its share delivery obligations to such subsequent purchasers minus (B) the average Draw Down Discount Price during the

applicable Draw Down Pricing Period. In the event that the Make Whole Amount is not paid within two (2) Trading Days following a demand therefor from the Investor, the Make Whole Amount shall accrue interest compounded daily at a rate of five percent (5%) per annum up to and including the date on which the Make Whole Amount is actually paid. Notwithstanding anything to the contrary set forth in this Agreement, in the event that the Company pays the Make Whole Amount (plus interest, if applicable) in respect of any Settlement Date in accordance with this Section 3.10, such payment shall be the Investor's sole remedy in respect of the Company's failure to deliver Shares in respect of such Settlement Date, the Company shall not be obligated to deliver such Shares and the Company shall not be deemed to be in breach of its obligations to the Investor in connection with the failure by the Company to deliver Shares to the Investor on a Settlement Date.

#### ARTICLE IV

##### REPRESENTATIONS AND WARRANTIES OF THE COMPANY

The Company hereby makes the following representations and warranties to the Investor:

Section 4.01. Organization, Good Standing and Power. The Company is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and has all the corporate power and authority to own, lease and operate its properties and to carry on its business as now being conducted. Except as set forth in the Commission Documents (as defined below), as of the Closing Date, the Company does not own more than fifty percent (50%) of the outstanding capital stock of or Control any other business entity, other than any wholly-owned subsidiary that is not "significant" within the meaning of Regulation S-X promulgated by the Commission. The Company is duly qualified as a foreign corporation to do business and is in good standing in every jurisdiction in which the nature of the business conducted or property owned by it makes such qualification necessary, other than those in which the failure so to qualify or be in good standing would not have a Material Adverse Effect.

Section 4.02. Authorization; Enforcement. (i) The Company has the requisite corporate power and authority to enter into and perform its obligations under this Agreement, the Registration Rights Agreement and the Warrant and to issue the Shares, the Warrant and the Warrant Shares as of their respective dates of issuance; (ii) the execution and delivery of this Agreement and the Registration Rights Agreement, and the execution, issuance and delivery of the Warrant, by the Company and the consummation by it of the transactions contemplated hereby and thereby have been duly authorized by all necessary corporate action and no further consent or authorization of the Company or its Board of Directors or stockholders is required (other than as contemplated by Section 6.05); and (iii) each of this Agreement and the Registration Rights Agreement has been duly executed and delivered, and the Warrant has been duly executed, issued and delivered, by the Company and constitute the valid and binding obligations of the Company enforceable against the Company in accordance with their respective terms, except as such enforceability may be limited by applicable bankruptcy, insolvency, or similar laws relating to, or affecting generally the enforcement of, creditors' rights and remedies or by other equitable principles of general application.

Section 4.03. Capitalization. The authorized capital stock of the Company and the shares thereof issued and outstanding as of December 31, 2003, are set forth on a Schedule previously delivered to the Investor. All of the outstanding shares of the Common Stock have been duly and validly authorized and issued, and are fully paid and non-assessable. Except as set forth in this Agreement or in the Commission Documents or as previously disclosed to the Investor in writing, as of the date hereof, no shares of Common Stock are entitled to preemptive rights or registration rights and there are no outstanding options, warrants, scrip, rights to subscribe to, call or commitments of any character whatsoever relating to, or securities or rights convertible into or exchangeable for or giving any right to subscribe for, any shares of capital stock of the Company. Except as set forth in this Agreement or in the Commission Documents or as previously disclosed to the Investor in writing, as of the date hereof, there are no contracts, commitments, understandings or arrangements by which the Company is or may become bound to issue additional shares of the capital stock of the Company or options, securities or rights convertible into or exchangeable for or giving any right to subscribe for any shares of capital stock of the Company. Except as previously disclosed to the Investor in writing or in the Commission Documents, as of the date hereof, the Company is not a party to any agreement granting registration rights to any Person with respect to any of its equity securities. Except as previously disclosed to the Investor in writing or in the Commission Documents, as of the Closing Date, the Company is not a party to, and it has no knowledge of, any agreement restricting the voting or transfer of any shares of the capital stock of the Company. The offer and sale of all capital stock, convertible securities, rights, warrants or options of the Company issued during the twenty-four month period immediately prior to the date hereof complied with all applicable federal and state securities laws, and to the knowledge of the Company, no stockholder has a right of rescission or damages with respect thereto that could reasonably be expected to have a Material Adverse Effect. The Company has furnished or made available to the Investor true and correct copies of the Company's Restated Certificate of Incorporation, as amended and in effect on the date hereof (the "Charter"), and the Company's Bylaws, as amended and in effect on the date hereof (the "Bylaws").

Section 4.04. Issuance of Shares. The Shares and the Warrant have been, and the Warrant Shares will be, duly authorized by all necessary corporate action and, when issued and paid for in accordance with the terms of this Agreement, the Registration Rights Agreement and the Warrant, the Shares and the Warrant Shares shall be validly issued and outstanding, fully paid and non-assessable, and the Investor shall be entitled to all rights accorded to a holder of shares of Common Stock as long as, and to the extent that, the Investor still owns any Shares.

Section 4.05. No Conflicts. The execution, delivery and performance of this Agreement, the Registration Rights Agreement, the Warrant and any other document or instrument contemplated hereby or thereby, by the Company and the consummation by the Company of the transactions contemplated hereby and thereby do not, except to an extent that would not have, individually or in the aggregate, a Material Adverse Effect: (i) violate any provision of the Charter or Bylaws; (ii) conflict with, or constitute a default (or an event which with notice or lapse of time or both would become a default) under, or give to others any rights of termination, amendment, acceleration or cancellation of, any material agreement, mortgage, deed of trust, indenture, note, bond, license, lease agreement, instrument or obligation to which the Company is a party; (iii) create or impose a lien, charge or encumbrance on any property of the Company under any agreement or any commitment to which the Company is a party or by which the Company is bound or by which any of its respective properties or

assets are bound; or (iv) result in a violation of any federal, state, local or foreign statute, rule, regulation, order, judgment or decree (including federal and state securities or blue sky laws and regulations) applicable to the Company or any of its subsidiaries or by which any property or asset of the Company or any of its subsidiaries are bound or affected. The Company is not required under federal, state or local law, rule or regulation to obtain any material consent, authorization or order of, or make any filing or registration with, any court or governmental agency in order for it to execute, deliver or perform any of its obligations under this Agreement, the Registration Rights Agreement or the Warrant, or issue and sell the Shares or the Warrant Shares in accordance with the terms hereof and thereof (other than any filings that may be required to be made by the Company with the Commission, the NASD/Nasdaq or state securities commissions subsequent to the Closing, and, any registration statement (including any amendment or supplement thereto) which may be filed pursuant hereto); provided, that for purposes of the representation made in this sentence, the Company is assuming and relying upon the accuracy of the relevant representations and agreements of the Investor herein.

Section 4.06. Commission Documents, Financial Statements. The Common Stock is registered pursuant to Section 12(b) or 12(g) of the Exchange Act and the Company has timely filed all reports, schedules, forms, statements and other documents required to be filed by it with the Commission pursuant to the reporting requirements of the Exchange Act, including materials filed pursuant to Section 13(a) or 15(d) of the Exchange Act (all of the foregoing, including filings incorporated by reference therein, being referred to herein as the "Commission Documents"). Except as previously disclosed to the Investor in writing, the Company has maintained all requirements for the continued listing or quotation of its Common Stock, and such Common Stock is currently listed or quoted on a Principal Market. The Company has made available to the Investor, or otherwise has made available on its website, true and complete copies of the Commission Documents filed with the Commission since December 31, 2002, and prior to the Closing Date. As of the date hereof, the Company has not provided to the Investor any information which, according to applicable law, rule or regulation, should have been disclosed publicly by the Company but which has not been so disclosed, other than with respect to the transactions contemplated by this Agreement. As of its date, the Company's Annual Report on Form 10-K for the year ended December 31, 2003, complied in all material respects with the requirements of the Exchange Act and the rules and regulations of the Commission promulgated thereunder applicable to such document, and, as of its date, after giving effect to the information disclosed and incorporated by reference therein, such Form 10-K did not contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary in order to make the statements therein, in light of the circumstances under which they were made, not misleading. As of their respective dates, the financial statements of the Company included in the Commission Documents filed with the Commission since December 31, 2002, complied as to form and substance in all material respects with applicable accounting requirements and the published rules and regulations of the Commission or other applicable rules and regulations with respect thereto. Such financial statements have been prepared in accordance with generally accepted accounting principles in the United States ("GAAP") applied on a consistent basis during the periods involved (except (i) as may be otherwise indicated in such financial statements or the notes thereto or (ii) in the case of unaudited interim statements, to the extent they may not include footnotes or may be condensed or summary statements), and fairly present in all material respects the financial position of the Company and its subsidiaries as of the dates thereof and the results of operations and cash flows for the periods then ended (subject, in the case of unaudited statements, to normal year-end audit adjustments).

Section 4.07. No Material Adverse Change. Except as disclosed in the Commission Documents, since March 31, 2004, no event or series of events has or have occurred that would, individually or in the aggregate, have a Material Adverse Effect on the Company.

Section 4.08. No Undisclosed Liabilities. Neither the Company nor any of its subsidiaries has any liabilities, obligations, claims or losses (whether liquidated or unliquidated, secured or unsecured, absolute, accrued, contingent or otherwise) that would be required to be disclosed on a balance sheet of the Company or any subsidiary (including the notes thereto) in conformity with GAAP and are not disclosed in the Commission Documents, other than those incurred in the ordinary course of the Company's or its subsidiaries respective businesses since December 31, 2003, and which, individually or in the aggregate, do not or would not have a Material Adverse Effect on the Company.

Section 4.09. No Undisclosed Events or Circumstances. To the Knowledge of the Company, no event or circumstance has occurred or exists with respect to the Company or its subsidiaries or their respective businesses, properties, operations or financial condition, which, under applicable law, rule or regulation, requires public disclosure or announcement by the Company but which has not been so publicly announced or disclosed and which, individually or in the aggregate, do not or would not have a Material Adverse Effect on the Company.

Section 4.10. Actions Pending. There is no action, suit, claim, investigation or proceeding pending or, to the Knowledge of the Company, threatened, against the Company or any subsidiary which questions the validity of this Agreement or the transactions contemplated hereby or any action taken or to be taken pursuant hereto or thereto. Except as set forth in the Commission Documents or on Schedule 4.10, there is no action, suit, claim, investigation or proceeding pending or, to the Knowledge of the Company, threatened, against or involving the Company, any subsidiary of the Company or any of their respective properties or assets that could be reasonably expected to have a Material Adverse Effect on the Company. Except as set forth in the Commission Documents or on Schedule 4.10, no judgment, order, writ, injunction or decree or award has been issued by or, so far as is known by the Company, requested of any court, arbitrator or governmental agency which might result in a Material Adverse Effect.

Section 4.11. Compliance with Law. The businesses of the Company and its subsidiaries have been and are presently being conducted in accordance with all applicable federal, state and local governmental laws, rules, regulations and ordinances, except as set forth in the Commission Documents or such that would not reasonably be expected to cause a Material Adverse Effect. Except as set forth in the Commission Documents, the Company and each of its subsidiaries have all franchises, permits, licenses, consents and other governmental or regulatory authorizations and approvals (collectively, "Consents") necessary for the conduct of its business as now being conducted by it, except for such franchises, permits, licenses, consents and other governmental or regulatory authorizations and approvals, the failure to possess which, individually or in the aggregate, could not reasonably be expected to have a Material Adverse Effect and no Consent contains a restriction on the Company or its subsidiaries that could reasonably be expected to have a Material Adverse Effect.

Section 4.12. Certain Fees. Except as expressly set forth in this Agreement, no brokers, finders or financial advisory fees or commissions will be payable by the Company or any of its subsidiaries in respect of the transactions contemplated by this Agreement.

Section 4.13. Disclosure. To the best of the Company's Knowledge, as of their respective dates, neither this Agreement nor the Schedules hereto nor the Registration Statement or the Warrant (as any of the foregoing may have been amended or supplemented after the date hereof) contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made herein or therein, in the light of the circumstances under which they were made herein or therein, not misleading.

Section 4.14. Material Non-Public Information. As of the date hereof, except for this Agreement and the transactions contemplated hereby, neither the Company nor its agents have disclosed to the Investor any material non-public information that, according to applicable law, rule or regulation, should have been disclosed publicly by the Company prior to the date hereof but which has not been so disclosed.

Section 4.15. Exemption from Registration; Valid Issuances. The issuance and sale of the Shares, the Warrant and the Warrant Shares in accordance with the terms, conditions and limitations of, and on the basis of the representations and warranties set forth in, this Agreement, the Warrant and the Registration Rights Agreement may be properly issued pursuant to Section 4(2), Regulation D and/or any other applicable federal and state securities or blue sky laws and regulations. Neither the sales of the Shares, the Warrant or the Warrant Shares pursuant to, nor the Company's performance of its obligations under, this Agreement, the Registration Rights Agreement or the Warrant, as applicable, shall (i) result in the creation or imposition of any liens, charges, claims or other encumbrances upon the Shares, the Warrant Shares or any of the assets of the Company or (ii) except as previously disclosed to the Investor in writing, entitle the holders of any outstanding shares of capital stock of the Company to preemptive or other rights to subscribe to or acquire the shares of Common Stock or other securities of the Company.

Section 4.16. No General Solicitation or Advertising in Regard to this Transaction. As of the date hereof, neither the Company nor any of its Affiliates or any person acting on its or their behalf (i) has conducted any general solicitation (as that term is used in Rule 502(c) of Regulation D) or general advertising with respect to any of the Shares, the Warrant or the Warrant Shares or (ii) has made any offers or sales of any security or solicited any offers to buy any security under any circumstances that would require registration of the Shares under the Securities Act.

Section 4.17. No Integrated Offering. Neither the Company, nor any of its Affiliates, nor any person acting on its or their behalf has, directly or indirectly, made any offers or sales of any security or solicited any offers to buy any security, other than pursuant to this Agreement and employee benefit plans, under circumstances that would require registration under the Securities Act of the Shares issuable hereunder with any other offers or sales of securities of the Company.



## ARTICLE V

### REPRESENTATIONS, WARRANTIES AND COVENANTS OF THE INVESTOR

The Investor hereby makes the following representations, warranties and covenants to the Company:

Section 5.01. Organization and Standing of the Investor. The Investor is a company duly organized, validly existing and in good standing under the laws of the British Virgin Islands.

Section 5.02. Authorization and Power. The Investor has the requisite power and authority to enter into and perform its obligations under this Agreement, the Registration Rights Agreement and the Warrant and to purchase or otherwise receive the Shares, the Warrant and the Warrant Shares in accordance with the terms hereof. The execution, delivery and performance of this Agreement by Investor and the consummation by it of the transactions contemplated hereby have been duly authorized by all necessary corporate action, and no further consent or authorization of the Investor, its Board of Directors or stockholders is required. This Agreement has been duly executed and delivered by the Investor and constitutes a valid and binding obligation of the Investor enforceable against the Investor in accordance with its terms, except as such enforceability may be limited by applicable bankruptcy, insolvency, reorganization, moratorium, liquidation, conservatorship, receivership or similar laws relating to, or affecting generally the enforcement of creditor's rights and remedies or by other equitable principles of general application.

Section 5.03. No Conflicts. The execution, delivery and performance of this Agreement, the Registration Rights Agreement, the Warrant and any other document or instrument contemplated hereby, by the Investor and the consummation of the transactions contemplated thereby do not (i) violate any provision of the Investor's charter documents or bylaws, (ii) conflict with, or constitute a default (or an event which with notice or lapse of time or both would become a default) under, or give to others any rights of termination, amendment, acceleration or cancellation of, any material agreement, mortgage, deed of trust, indenture, note, bond, license, lease agreement, instrument or obligation to which the Investor is a party, (iii) create or impose a lien, charge or encumbrance on any property of the Investor under any agreement or any commitment to which the Investor is a party or by which the Investor is bound or by which any of its respective properties or assets are bound or (iv) result in a violation of any federal, state, local or foreign statute, rule, regulation, order, judgment or decree (including federal and state securities laws and regulations) applicable to the Investor or by which any property or asset of the Investor are bound or affected, except in all cases, for such conflicts, defaults, terminations, amendments, accelerations, cancellations and violations as would not, individually or in the aggregate, prohibit or otherwise interfere with the ability of the Investor to enter into and perform its obligations under this Agreement in any material respect. The Investor is not required under federal, state or local law, rule or regulation to obtain any consent, authorization or order of, or make any filing or registration with, any court or governmental agency in order for it to execute, deliver or perform any of its obligations under this Agreement or to purchase the Shares or the Warrant in accordance with the terms hereof; provided, that for purposes of the representation made in this sentence, the Investor is assuming and relying upon the accuracy of the relevant representations and agreements of the Company herein.

Section 5.04. Financial Capability; Accredited Investor. The Investor has the financial capability to perform all of its obligations under this Agreement, including the capability to purchase the Shares, the Warrant and the Warrant Shares in accordance with the terms hereof. The Investor is an "Accredited Investor" as defined in Rule 501 of Regulation D. The Investor is aware of the Company's business affairs and financial condition and has had sufficient access to and has acquired sufficient information about the Company to reach an informed and knowledgeable decision to acquire the Shares, the Warrant and the Warrant Shares. The Investor has such business and financial experience as is required to give it the capacity to utilize the information received, to evaluate the risks involved in purchasing the Shares, the Warrant and the Warrant Shares, to make an informed decision about purchasing the Shares, the Warrant and the Warrant Shares and to protect its own interests in connection with the purchase of the Shares, the Warrant and the Warrant Shares and is able to bear the risks of an investment in the Shares, the Warrant and the Warrant Shares. The Investor is not an Affiliate of the Company.

Section 5.05. Information. The Investor and its advisors, if any, have been furnished with all materials relating to the business, finances and operations of the Company and materials relating to the offer and sale of the Shares, the Warrant and the Warrant Shares which have been requested by the Investor. The Investor and its advisors, if any, have been afforded the opportunity to ask questions of the Company. The Investor has sought such accounting, legal and tax advice as it has considered necessary to make an informed investment decision with respect to its acquisition of the Shares, the Warrant and the Warrant Shares. The Investor understands that it (and not the Company) shall be responsible for its own tax liabilities that may arise as a result of this investment or the transactions contemplated by this Agreement.

Section 5.06. Selling Restrictions. The Investor covenants that during the Commitment Period, neither the Investor nor any of its Affiliates nor any entity managed by the Investor (i) will ever, through related parties or otherwise, (X) purchase, trade, offer, pledge, sell, contract to sell or to purchase or sell or "short" or "short against the box" (as those terms are generally understood in the securities markets), or otherwise dispose of or acquire, any derivative securities of the Company or options in respect of such securities, including, but not limited to, by way of option or equity swap transactions in or with respect to the Company's Common Stock or any other derivative security transaction or (Y) upon receipt by the Investor of any Draw Down Notice from the Company, sell or contract to sell any shares of Common Stock (other than any shares of Common Stock purchased by the Investor pursuant to any Draw Down Notice under this Agreement) until the end of the Draw Down Pricing Period set forth in such Draw Down Notice or (ii) will ever, through related parties or otherwise, engage in any transaction intended to reduce the economic risk of ownership of shares of Common Stock (including, without limitation, the purchase of any option or contract to sell) that would, directly or indirectly, have an effect substantially equivalent to selling short such shares of Common Stock that are subject to, underlie or may be deliverable in satisfaction of such transaction or otherwise may be reasonably be expected to adversely affect the market price of the Common Stock. For the sake of clarity, the Investor shall have the right at any time, including during any Draw Down Pricing Period, to sell any shares of Common Stock purchased by the Investor pursuant to any Draw Down Notice under this Agreement.

Section 5.07. Statutory Underwriter Status. The Investor acknowledges and agrees that, pursuant to the Commission's current interpretations of the Securities Act, the Investor will be disclosed as an "underwriter" within the meaning of the Securities Act in the Registration Statement (and any amendments or supplements thereto) and in any Prospectus contained therein to the extent required by applicable law.

Section 5.08. Compliance with Insider Trading Rules. The Investor acknowledges and agrees that it is aware, and that it will advise each of its Affiliates and representatives that is provided any confidential information of the Company, that the United States securities laws and regulations provide that any person who has received directly or indirectly from an issuer such as the Company material, non-public information is prohibited from purchasing or selling securities of such issuer or from communicating such information to any other person under circumstances in which it is reasonably foreseeable that such person is likely to purchase or sell such securities. The Investor further agrees not to provide any Person with material, nonpublic information received from the Company or its representatives, including any relative, associate or other individual who intends to, or may, (a) trade securities with respect to the Company which is the subject of such information or (b) otherwise directly or indirectly benefit from such information.

## ARTICLE VI

### COVENANTS OF THE COMPANY

The Company covenants to the Investor as follows, which covenants are for the sole benefit of the Investor and its permitted assignees (as defined herein):

Section 6.01. Securities. The Company shall notify the Commission and the Principal Market, if and as applicable, in accordance with their rules and regulations, of the transactions contemplated by this Agreement, and shall use commercially reasonable efforts to take all other necessary action and proceedings as may be required and permitted by applicable law, rule or regulation, for the legal and valid issuance of the Shares and the Warrant Shares, if any, to the Investor.

Section 6.02. Reservation of Common Stock. As of the date hereof, the Company has available and the Company shall reserve and keep available at all times, free of preemptive rights and other similar contractual rights of stockholders, shares of Common Stock for the purpose of enabling the Company to satisfy any obligation to issue the Shares in connection with all Draw Downs contemplated hereunder and the Warrant Shares. The number of shares so reserved from time to time, as theretofore increased or reduced as hereinafter provided, may be reduced by the number of shares actually delivered hereunder.

Section 6.03. Registration and Listing. During the Commitment Period, the Company shall use commercially reasonable efforts: (i) to take all action necessary to cause its Common Stock to continue to be registered under Section 12(b) or 12(g) of the Exchange Act; (ii) to comply in all material respects with its reporting and filing obligations under the Exchange Act; and (iii) to prevent the termination or suspension such registration, or the termination or suspension of its reporting and filing obligations under the Exchange Act or Securities Act (except as expressly permitted herein). The Company shall use commercially reasonable efforts necessary to maintain the listing and trading of its Common Stock and the listing of the Shares purchased by Investor hereunder on a Principal Market (including, without limitation, maintaining sufficient net tangible assets) and will comply in all material respects with the Company's reporting, filing and other obligations under the bylaws or rules of the applicable Principal Market.

Section 6.04. Registration Statement. Without the prior written consent of the Investor, the Registration Statement shall be used solely in connection with the transactions between the Company and the Investor contemplated hereby.

Section 6.05. Compliance with Laws.

(a) The Company shall, and cause each subsidiary to, comply, in all material respects, with all applicable laws, rules, regulations and orders, the noncompliance with which could reasonably be expected to have a Material Adverse Effect.

(b) Without the consent of its stockholders in accordance with the rules of the applicable Principal Market, the Company will not be obligated to issue, and the Investor will not be obligated to purchase, any Shares which would result in the issuance under this Agreement of Shares representing more than the applicable percentage under the rules of the applicable Principal Market that would require stockholder approval of the issuance thereof.

Section 6.06. Reporting Requirements. Unless otherwise available to the public by way of the Commission's Electronic Document Gathering, Analysis, and Retrieval system ("EDGAR"), upon reasonable written request of the Investor during the Commitment Period, the Company shall furnish copies of the following to the Investor within three Trading Days of such request (but not sooner than filed with or submitted to the Commission):

- (a) Quarterly Reports on Form 10-Q;
- (b) Annual Reports on Form 10-K;
- (c) Periodic Reports on Form 8-K; and
- (d) any other documents publicly furnished or submitted to the Commission.

Section 6.07. Other Financing. The Company may, without the prior written consent of the Investor, (i) establish stock option or award plans or agreements (for directors, employees, consultants and/or advisors), and issue securities thereunder, and amend such plans or agreements, including increasing the number of shares available thereunder, (ii) use equity securities to finance, or otherwise in connection with, the acquisition of one or more other companies, equipment, technologies or lines of business, (iii) issue shares of Common Stock and/or preferred stock in connection with the Company's option or award plans, stock purchase plans, rights plans, warrants or options, (iv) issue shares of Common Stock and/or Preferred Stock in connection with the acquisition of products, licenses, equipment or other assets and strategic alliances or partnerships or joint ventures (the primary purpose of which is not to raise equity capital); (v) issue shares of Common and/or Preferred Stock to consultants and/or advisors as consideration for services rendered, (vi) issue and sell equity or debt or hybrid securities in a public offering, (vii) issue and sell equity or debt or hybrid securities in a private placement (other than in connection with any Prohibited Transaction), (viii) issue equity securities to equipment lessors, equipment vendors, banks or similar lending institutions in connection with leases or loans, or in connection with strategic commercial

or licensing transactions, (ix) issue securities in connection with any stock split, stock dividend, recapitalization, reclassification or similar event by the Company, (x) issue shares of Common Stock to the Investor under any other agreement entered into between the Investor and the Company and (xi) enter into any other transaction that is not a Prohibited Transaction (each a "Permitted Transaction"). The Company shall use commercially reasonable efforts to notify the Investor in writing prior to the consummation of any material Permitted Transaction described in clauses (vi), (vii) or (ix) above.

Section 6.08. Prohibited Transactions. During the term of this Agreement, the Company shall not enter into any Prohibited Transaction without the prior written consent of the Investor, which consent may be withheld at the sole discretion of the Investor; provided, however, that the Investor agrees that it will grant such consent if it determines in its sole discretion, acting in good faith, that the Prohibited Transaction is not reasonably likely to materially interfere with its rights and obligations under this Agreement. For the purposes of this Agreement, the term "Prohibited Transaction" shall refer to the issuance by the Company of any "future priced securities," which shall be deemed to mean the issuance of shares of Common Stock or securities of any type whatsoever that are, or may become, convertible or exchangeable into shares of Common Stock where the purchase, conversion or exchange price for such Common Stock is determined using any floating or otherwise adjustable discount to the market price of the Common Stock, including, without limitation, pursuant to any equity line or other financing that is substantially similar to the financing provided under this Agreement; provided, however, that nothing in this Section 6.08 shall prohibit the Company from issuing any securities of any type that are, or may become, convertible or exchangeable into shares of Common Stock with a fixed or determined purchase, conversion or exchange price (and which may be accompanied by anti-dilution provisions), which price may be at a discount to the market price of Common Stock.

Section 6.09. Corporate Existence. The Company shall take all steps necessary to preserve and continue the corporate existence of the Company; provided, however, that nothing in this Agreement shall be deemed to prohibit the Company from engaging in any merger, consolidation, sale of all or substantially all of its assets or similar transaction with another Person pursuant to which such other Person is the surviving entity in the transaction.

Section 6.10. Non-Disclosure of Non-Public Information. Except as set forth in Section 6.11 and 6.12, none of the Company, its officers, directors, employees nor agents shall disclose material non-public information to the Investor, its advisors or representatives.

Section 6.11. Notice of Certain Events Affecting Registration; Suspension of Right to Request a Draw Down. Notwithstanding the provisions of Section 6.10, the Company shall immediately notify the Investor upon the occurrence of any of the following events in respect of the Registration Statement or the Prospectus related to the offer, issuance and sale of the Shares and the Warrant Shares hereunder: (i) receipt of any request for additional information by the Commission or any other federal or state governmental authority during the period of effectiveness of the Registration Statement for amendments or supplements to the Registration Statement or the Prospectus; (ii) the issuance by the Commission or any other federal or state governmental authority of any stop order suspending the effectiveness of the Registration Statement or the initiation of any proceedings for that purpose; or (iii) receipt of any notification with respect to the suspension of the qualification or exemption from qualification of any of the Registrable Securities for sale in any jurisdiction or the initiation or threatening of any proceeding for such purpose. The Company shall not request a Draw Down during the continuation of any of the foregoing events.

Section 6.12. Amendments to the Registration Statement. Notwithstanding the provisions set forth in Section 6.10, if the Registration Statement is declared effective by the Commission, the Company shall not (i) file any amendment to the Registration Statement or make any amendment or supplement to the Prospectus of which the Investor shall not previously have been advised or to which the Investor shall reasonably object after being so advised or (ii) so long as, in the reasonable opinion of counsel for the Investor, a Prospectus is required to be delivered in connection with sales of the Shares by the Investor, file any information, documents or reports pursuant to the Exchange Act without delivering a copy of such information, documents or reports to the Investor promptly following such filing unless such information, documents or reports are available by way of EDGAR.

Section 6.13. Prospectus Delivery. From time to time for such period as in the opinion of counsel for the Investor a prospectus is required by the Securities Act to be delivered in connection with sales by the Investor, the Company will expeditiously deliver to the Investor, without charge, as many copies of the Prospectus (and of any amendment or supplement thereto) as the Investor may reasonably request. The Company consents to the use of the Prospectus (and of any amendment or supplement thereto) in accordance with the provisions of the Securities Act and state securities laws in connection with the offering and sale of the Shares and the Warrant Shares and for such period of time thereafter as the Prospectus is required by the Securities Act to be delivered in connection with sales of the Shares and the Warrant Shares.

#### ARTICLE VII

##### CONDITIONS TO THE OBLIGATION OF THE INVESTOR TO ACCEPT A DRAW DOWN

The obligation of the Investor hereunder to accept a Draw Down Notice and to acquire and pay for the Shares in accordance therewith is subject to the satisfaction or waiver, at each Condition Satisfaction Date, of each of the conditions set forth below. The conditions are for the Investor's sole benefit and may be waived by the Investor at any time in its sole discretion. As used in this Agreement, the term "Condition Satisfaction Date" shall mean, with respect to each Draw Down, the date on which the applicable Draw Down Notice is delivered to the Investor and each Settlement Date in respect of the applicable Draw Down Pricing Period.

Section 7.01. Accuracy of the Company's Representations and Warranties. Each of the representations and warranties of the Company in this Agreement shall be true and correct in all material respects as though made on and as of such Condition Satisfaction Date, except for such representations and warranties that are expressly made as of a particular date.

Section 7.02. Performance by the Company. The Company shall have performed, satisfied and complied in all material respects with all covenants, agreements and conditions required by this Agreement, the Registration Rights Agreement and the Warrant required to be performed, satisfied or complied with by the Company as of or prior to the applicable Condition Satisfaction Date.

Section 7.03. Compliance with Law. The Company shall have complied in all material respects with all applicable federal, state and local governmental laws, rules, regulations and ordinances in connection with the execution, delivery and performance of this Agreement and the consummation of the transactions contemplated hereby.

Section 7.04. Effective Registration Statement. Upon the terms and subject to the conditions and limitations set forth in the Registration Rights Agreement, the Registration Statement shall have previously become effective and shall remain effective and (i) neither the Company nor the Investor shall have received notice that the Commission has issued or intends to issue a stop order with respect to the Registration Statement or that the Commission otherwise has suspended or withdrawn the effectiveness of the Registration Statement, either temporarily or permanently, or intends or has threatened to do so (unless the Commission's concerns have been addressed and the Investor is reasonably satisfied that the Commission no longer is considering or intends to take such action), and (ii) no other suspension of the use or withdrawal of the effectiveness of the Registration Statement or the Prospectus shall exist.

Section 7.05. No Knowledge. The Company shall have no Knowledge of any event more likely than not to have the effect of causing the Registration Statement with respect to the resale of the Registrable Securities by the Investor to be suspended or otherwise ineffective (which event is more likely than not to occur within fifteen (15) Trading Days following the Trading Day on which a Draw Down Notice is delivered).

Section 7.06. No Suspension. Trading in the Common Stock shall not have been suspended by the Commission or the applicable Principal Market and trading in securities generally as reported on the applicable Principal Market shall not have been suspended or limited.

Section 7.07. No Injunction. No statute, rule, regulation, executive order, decree, ruling or injunction shall have been enacted, entered, promulgated or endorsed by any court or governmental authority of competent jurisdiction which prohibits the consummation of any of the transactions contemplated by this Agreement.

Section 7.08. No Proceedings or Litigation. No action, suit or proceeding before any arbitrator or any governmental authority shall have been commenced, and no investigation by any governmental authority shall have been threatened, against the Company or any subsidiary, or any of the officers, directors or Affiliates of the Company or any subsidiary seeking to enjoin, prevent or change the transactions contemplated by this Agreement.

Section 7.09. Section 16 Limitation. On each Settlement Date, the number of Shares then to be purchased by the Investor shall not exceed the number of such shares that, when aggregated with all other Registrable Securities then owned by the Investor beneficially or deemed beneficially owned by the Investor, would result in the Investor owning more than 9.9% of all of such Common Stock as would be outstanding on such Settlement Date, as determined in accordance with Section 16 of the Exchange Act. For purposes of this Section 7.09, in the event that the amount of Common Stock outstanding as determined in accordance

with Section 16 of the Exchange Act and the regulations promulgated thereunder is greater on a Settlement Date than on the date upon which the Draw Down Notice associated with such Settlement Date is given, the amount of Common Stock outstanding on such Settlement Date shall govern for purposes of determining whether the Investor, when aggregating all purchases of Common Stock made pursuant to this Agreement and, if any, Warrant Shares, would own more than 9.9% of the Common Stock following such Settlement Date.

Section 7.10. Sufficient Shares Registered for Resale. The Company shall have sufficient Shares, calculated using the closing trade price of the Common Stock as of the Trading Day immediately preceding such Draw Down Notice, registered under the Registration Statement to issue and sell the Shares purchased in connection with each Draw Down Notice.

Section 7.11. Warrant. The Warrant shall have been duly executed, delivered and issued to the Investor, and the Company shall not be in default in any material respect under any of the provisions thereof, provided that any refusal by or failure of the Company to issue and deliver Warrant Shares in respect of any exercise (in whole or in part) thereof shall be deemed to be material for the purposes of this Section 7.11.

Section 7.12. Opinion of Counsel. The Investor shall have received an opinion of counsel to the Company, dated as of the Closing Date, in form and substance reasonably satisfactory to the Investor and its counsel substantially in the form attached hereto as Exhibit D.

## ARTICLE VIII

### LEGENDS

Section 8.01. Legends. Unless otherwise provided below, each certificate representing Registrable Securities will bear the following legend (the "Legend"):

THE SECURITIES EVIDENCED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), OR ANY OTHER APPLICABLE SECURITIES LAWS AND HAVE BEEN ISSUED IN RELIANCE UPON AN EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND SUCH OTHER SECURITIES LAWS. NEITHER THIS SECURITY NOR ANY INTEREST OR PARTICIPATION HEREIN MAY BE REOFFERED, SOLD, ASSIGNED, TRANSFERRED, PLEDGED, ENCUMBERED, HYPOTHECATED OR OTHERWISE DISPOSED OF, EXCEPT PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT OR PURSUANT TO A TRANSACTION THAT IS EXEMPT FROM, OR NOT SUBJECT TO, SUCH REGISTRATION. THE HOLDER OF THIS CERTIFICATE IS THE BENEFICIARY OF CERTAIN OBLIGATIONS OF THE COMPANY SET FORTH IN A COMMON STOCK PURCHASE AGREEMENT BETWEEN DISCOVERY LABORATORIES, INC., AND KINGSBRIDGE CAPITAL LIMITED DATED AS OF JULY 7, 2004. A COPY OF THE PORTION OF THE AFORESAID AGREEMENT EVIDENCING SUCH OBLIGATIONS MAY BE OBTAINED FROM THE COMPANY'S EXECUTIVE OFFICES.



As soon as practicable after the execution and delivery hereof, but in any event within five (5) Trading Days thereafter, the Company shall issue to the transfer agent for its Common Stock (and to any substitute or replacement transfer agent for its Common Stock upon the Company's appointment of any such substitute or replacement transfer agent) instructions, with a copy to the Investor. It is the intent and purpose of such instructions, as provided therein, to require the transfer agent for the Common Stock from time to time upon transfer of Registrable Securities by the Investor to issue certificates evidencing such Registrable Securities free of the Legend during the following periods and under the following circumstances and without consultation by the transfer agent with the Company or its counsel and without the need for any further advice or instruction or documentation to the transfer agent by or from the Company or its counsel or the Investor, unless an opinion of Investor's counsel is reasonably required by the transfer agent or the Company:

(a) At any time after the Closing Date to the extent accompanied by a notice requesting the issuance of certificates free of the Legend; provided, that (i) the Company is reasonably able to confirm to the transfer agent that the Registration Statement shall then be effective and (ii) if reasonably requested by the transfer agent the Investor confirms to the transfer agent that the Investor has complied with the prospectus delivery requirement under the Securities Act.

(b) At any time upon any surrender of one or more certificates evidencing Registrable Securities that bear the Legend, to the extent accompanied by a notice requesting the issuance of new certificates free of the Legend to replace those surrendered and containing representations that (i) the Investor is permitted to dispose of such Registrable Securities without limitation as to amount or manner of sale pursuant to Rule 144(k) under the Securities Act and there is no requirement for the Investor to deliver a prospectus or (ii) the Investor has sold, pledged or otherwise transferred or agreed to sell, pledge or otherwise transfer such Registrable Securities in a manner other than pursuant to an effective registration statement, to a transferee who shall upon such transfer be entitled to freely tradable securities.

Section 8.02. No Other Legend or Stock Transfer Restrictions. No legend other than the one specified in Section 8.01 has been or shall be placed on the share certificates representing the Common Stock issued to the Investor and no instructions or "stop transfer orders," so called "stock transfer restrictions," or other restrictions have been or shall be given to the Company's transfer agent with respect thereto other than as expressly set forth in this Article VIII.

## ARTICLE IX

### TERMINATION

Section 9.01. Term. Unless otherwise terminated in accordance with Section 9.02 below, this Agreement shall terminate upon the expiration of the Commitment Period.

Section 9.02. Other Termination.

(a) The Investor may terminate this Agreement upon (x) one (1) day's notice if the Company enters into any Prohibited Transaction as set forth in Section 6.08 without the Investor's prior written consent, or (y) one (1) day's notice within ten (10) Trading Days after the Investor obtains actual knowledge that an event resulting in a Material Adverse Effect has occurred; provided, however, that the Investor shall be deemed to possess such actual knowledge within five (5) Trading Days after such event has been publicly disclosed by the Company in accordance with its periodic reporting requirements under the Exchange Act.

(b) The Investor may terminate this Agreement upon one (1) day's notice to the Company at any time in the event that the Registration Statement is not declared effective in accordance with the Registration Rights Agreement.

(c) The Company may terminate this Agreement upon one (1) day's notice; provided, however, that the Company shall not terminate this Agreement pursuant to this Section 9.02(c) during any Draw Down Pricing Period; provided, further, that in the event of any termination of this Agreement by the Company hereunder, so long as the Investor owns Shares purchased hereunder and/or Warrant Shares, unless all of such shares of Common Stock may be resold by the Investor without registration and without any time, volume or manner limitations pursuant to Rule 144(k) (or any similar provision then in effect) under the Securities Act, the Company shall not suspend or withdraw the Registration Statement or otherwise cause the Registration Statement to become ineffective, or voluntarily delist the Common Stock from the applicable Principal Market, without listing the Common Stock on another Principal Market.

(d) Each of the parties hereto may terminate this Agreement upon one (1) day's notice if the other party has breached a material representation, warranty or covenant to this Agreement and such breach is not remedied within ten (10) Trading Days after notice of such breach is delivered to the breaching party.

(e) The obligation of the Investor to purchase shares of Common Stock shall terminate permanently in the event that there shall occur any stop order or suspension of effectiveness of the Registration Statement for an aggregate of thirty (30) calendar days during the Commitment Period.

(f) In the event of termination by the Company or the Investor, written notice thereof shall forthwith be given to the other party and the transactions contemplated by this Agreement shall be terminated without further action by either party. If this Agreement is terminated as provided in Section 9.01 or 9.02 herein, this Agreement shall become void and of no further force and effect, except as provided in Section 12.14. Nothing in this Section 9.03 shall be deemed to release the Company or the Investor from any liability for any breach under this Agreement or to impair the rights of the Company and the Investor to compel specific performance by the other party of its obligations under this Agreement.

## ARTICLE X

### INDEMNIFICATION

#### Section 10.01. Indemnification.

(a) Except as otherwise provided in this Article X, unless disputed as set forth in Section 10.02, the Company agrees to indemnify, defend and hold harmless the Investor and its Affiliates and their respective officers, directors, agents, employees, subsidiaries, partners, members and Controlling persons (each, an "Investor Indemnified Party"), to the fullest extent permitted by law from and against any and all Damages directly resulting from or directly arising out of any breach of any representation or warranty, covenant or agreement by the Company in this Agreement, the Registration Rights Agreement or the Warrant; provided, however, that the Company shall not be liable under this Article X to an Investor Indemnified Party to the extent that such Damages resulted or arose from the breach by an Investor Indemnified Party of any representation, warranty, covenant or agreement of an Investor Indemnified Party contained in this Agreement, the Registration Rights Agreement or the Warrant or the gross negligence, recklessness, willful misconduct or bad faith of an Investor Indemnified Party. The parties intend that any Damages subject to indemnification pursuant to this Article X will be net of insurance proceeds (which the Investor Indemnified Party agrees to use commercially reasonable efforts to recover). Accordingly, the amount which the Company is required to pay to any Investor Indemnified Party hereunder (a "Company Indemnity Payment") will be reduced by any insurance proceeds actually recovered by or on behalf of any Investor Indemnified Party in reduction of the related Damages. In addition, if an Investor Indemnified Party receives a Company Indemnity Payment required by this Article X in respect of any Damages and subsequently receives any such insurance proceeds, then the Investor Indemnified Party will pay to the Company an amount equal to the Company Indemnity Payment received less the amount of the Company Indemnity Payment that would have been due if the insurance proceeds had been received, realized or recovered before the Company Indemnity Payment was made.

(b) Except as otherwise provided in this Article X, unless disputed as set forth in Section 10.02, the Investor agrees to indemnify, defend and hold harmless the Company and its subsidiaries and Affiliates and their respective officers, directors, agents, employees, subsidiaries, partners, members and Controlling persons (each, a "Company Indemnified Party"), to the fullest extent permitted by law from and against any and all Damages directly resulting from or arising out of any breach of any representation or warranty, covenant or agreement by the Investor in this Agreement, the Registration Right Agreement or the Warrant; provided, however, that the Investor shall not be liable under this Article X to a Company Indemnified Party to the extent that such Damages resulted or arose from the breach by a Company Indemnified Party of any representation, warranty, covenant or agreement of a Company Indemnified Party contained in this Agreement, the Registration Right Agreement or the Warrant or gross negligence, recklessness, willful misconduct or bad faith of a Company Indemnified Party. The parties intend that any Damages subject to indemnification pursuant to this Article X will be net of insurance proceeds (which the Company agrees to use commercially reasonable efforts to recover). Accordingly, the amount which the Investor is required to pay to any Company Indemnified Party hereunder (an "Investor Indemnity Payment") will be reduced by any insurance proceeds theretofore actually recovered by or on behalf of any Company Indemnified Party in reduction of the related Damages. In addition, if a Company Indemnified Party receives a Investor Indemnity Payment required by this Article X in respect of any Damages and subsequently receives insurance such proceeds, then the Company Indemnified Party will pay to the Investor an amount equal to the Investor Indemnity Payment received less the amount of the Investor Indemnity Payment that would have been due if the insurance proceeds had been received, realized or recovered before the Investor Indemnity Payment was made.

Section 10.02. Notification of Claims for Indemnification. Each party entitled to indemnification under this Article X (an "Indemnified Party") shall, promptly after the receipt of notice of the commencement of any claim against such Indemnified Party in respect of which indemnity may be sought from the party obligated to indemnify such Indemnified Party under this Article X (the "Indemnifying Party"), notify the Indemnifying Party in writing of the commencement thereof. Any such notice shall describe the claim in reasonable detail. The failure of any Indemnified Party to so notify the Indemnifying Party of any such action shall not relieve the Indemnifying Party from any liability which it may have to such Indemnified Party (a) other than pursuant to this Article X or (b) under this Article X unless, and only to the extent that, such failure results in the Indemnifying Party's forfeiture of substantive rights or defenses or the Indemnifying Party is prejudiced by such delay. The procedures listed below shall govern the procedures for the handling of indemnification claims.

(a) Any claim for indemnification for Damages that do not result from a Third Party Claim as defined in the following paragraph, shall be asserted by written notice given by the Indemnified Party to the Indemnifying Party. Such Indemnifying Party shall have a period of thirty (30) days after the receipt of such notice within which to respond thereto. If such Indemnifying Party does not respond within such thirty (30) day period, such Indemnifying Party shall be deemed to have refused to accept responsibility to make payment as set forth in Section 10.01. If such Indemnifying Party does not respond within such thirty (30) day period or rejects such claim in whole or in part, the Indemnified Party shall be free to pursue such remedies as specified in this Agreement, including the dispute resolution provisions set forth in Section 10.03 below.

(b) If an Indemnified Party shall receive notice or otherwise learn of the assertion by a person or entity not a party to this Agreement of any threatened legal action or claim (collectively a "Third Party Claim"), with respect to which an Indemnifying Party may be obligated to provide indemnification, the Indemnified Party shall give such Indemnifying Party written notice thereof within twenty (20) days after becoming aware of such Third Party Claim.

(c) An Indemnifying Party may elect to defend (and, unless the Indemnifying Party has specified any reservations or exceptions, to seek to settle or compromise) at such Indemnifying Party's own expense and by such Indemnifying Party's own counsel, any Third Party Claim. Within thirty (30) days after the receipt of notice from an Indemnified Party (or sooner if the nature of such Third Party Claim so requires), the Indemnifying Party shall notify the Indemnified Party whether the Indemnifying Party will assume responsibility for defending such Third Party Claim, which election shall specify any reservations or exceptions. If such Indemnifying Party does not respond within such thirty (30) day period or rejects such claim in whole or in part, the Indemnified Party shall be free to pursue such remedies as specified in this Agreement, including the dispute resolution provisions set forth in Section 10.03 below. In case any such Third Party Claim shall be brought against any Indemnified Party, and it shall notify the Indemnifying Party of the commencement thereof, the

Indemnifying Party shall be entitled to assume the defense thereof at its own expense, with counsel satisfactory to such Indemnified Party in its reasonable judgment; provided, however, that any Indemnified Party may, at its own expense, retain separate counsel to participate in such defense at its own expense. Notwithstanding the foregoing, in any Third Party Claim in which both the Indemnifying Party, on the one hand, and an Indemnified Party, on the other hand, are, or are reasonably likely to become, a party, such Indemnified Party shall have the right to employ separate counsel and to control its own defense of such claim if, in the reasonable opinion of counsel to such Indemnified Party, either (x) one or more significant defenses are available to the Indemnified Party that are not available to the Indemnifying Party or (y) a conflict or potential conflict exists between the Indemnifying Party, on the one hand, and such Indemnified Party, on the other hand, that would make such separate representation advisable; provided, however, that in such circumstances the Indemnifying Party (i) shall not be liable for the fees and expenses of more than one counsel to all Indemnified Parties and (ii) shall reimburse the Indemnified Parties for such reasonable fees and expenses of such counsel incurred in any such Third Party Claim, as such expenses are incurred, provided that the Indemnified Parties agree to repay such amounts if it is ultimately determined that the Indemnifying Party was not obligated to provide indemnification under this Article X. The Indemnifying Party agrees that it will not, without the prior written consent of the Indemnified Party, settle, compromise or consent to the entry of any judgment in any pending or threatened claim relating to the matters contemplated hereby (if any Indemnified Party is a party thereto or has been actually threatened to be made a party thereto) unless such settlement, compromise or consent includes an unconditional release of such Indemnified Party from all liability arising or that may arise out of such claim. The Indemnifying Party shall not be liable for any settlement of any claim effected against an Indemnified Party without the Indemnifying Party's written consent, which consent shall not be unreasonably withheld, conditioned or delayed. The rights accorded to an Indemnified Party hereunder shall be in addition to any rights that any Indemnified Party may have at common law, by separate agreement or otherwise (subject, however, to the provisions of Section 10.03 below); provided, however, that notwithstanding the foregoing or anything to the contrary contained in this Agreement, nothing in this Article X (other than Section 10.03) shall restrict or limit any rights that any Indemnified Party may have to seek equitable relief.

## ARTICLE XI

### ARBITRATION

Section 11.01. Arbitration. Any dispute under this Agreement, the Registration Rights Agreement or the Warrant shall be submitted to arbitration (including, without limitation, pursuant to this Article X) by sending written notice of such election to the other party or parties clearly marked "Arbitration Demand". Thereupon such dispute shall be arbitrated in accordance with the terms and conditions of this Article XI. Notwithstanding the foregoing, either party, subject to the terms, conditions and provisions of Section 12.12, may apply to a court of competent jurisdiction for a temporary restraining order, a preliminary injunction or other equitable relief to preserve the status quo or prevent irreparable harm.

Section 11.02. Board of Arbitration. Each of the Company and the Investor shall select one (1) member of the Board of Arbitration and the third member shall be selected by mutual agreement of the other members, or if the other members fail to reach agreement on a third member within twenty (20) days after their selection, such third member shall thereafter be selected by the American Arbitration Association upon application made to it for such purpose by either party to this Agreement.

Section 11.03. Counterclaims. Nothing contained herein shall operate to prevent either party from asserting counterclaim(s) in any arbitration commenced in accordance with this Agreement, and any such party need not comply with the procedural provisions of this Article XI in order to assert such counterclaim(s).

Section 11.04. Procedures. The arbitration shall be filed with the office of the American Arbitration Association ("AAA") located in Wilmington, Delaware or such other AAA office as the parties may agree upon (without any obligation to so agree). The arbitration shall be conducted pursuant to the Commercial Arbitration Rules of AAA as in effect at the time of the arbitration hearing, such arbitration to be completed in a 60-day period. In addition, the following rules and procedures shall apply to the arbitration:

(a) The Board of Arbitration shall meet on consecutive business days in the city in which the arbitration was filed, and shall reach and render a decision (concurrent in by a majority of the members of the Board of Arbitration) which shall be in writing and state the findings the facts and conclusions of law upon which the decision is based, shall be final and binding upon the parties, who shall forthwith comply after receipt thereof. In connection with rendering its decisions, the Board of Arbitration shall adopt and follow such rules and procedures as a majority of the members of the Board of Arbitration deems necessary or appropriate. To the extent practical, decisions of the Board of Arbitration shall be rendered no more than thirty (30) calendar days following commencement of proceedings with respect thereto. The Board of Arbitration shall cause its written decision to be delivered to the parties hereto that are involved in such arbitration. Any decision made by the Board of Arbitration (either prior to or after the expiration of such thirty (30) calendar day period) shall be final, binding and conclusive on the Indemnified Party and the Indemnifying Party and entitled to be enforced to the fullest extent permitted by law and entered in any court of competent jurisdiction. Each party submits itself to the jurisdiction of any such court, but only for the entry and enforcement to judgment with respect to the decision of the arbitrator hereunder.

(b) The Board of Arbitration shall have the sole authority to decide whether or not any dispute between the parties is arbitrable and whether the party presenting the issues to be arbitrated has satisfied the conditions precedent to such party's right to commence arbitration as required by this Article XI.

(c) The Board of Arbitration shall have the power to grant all legal and equitable remedies (including, without limitation, specific performance) and award compensatory damages provided by applicable law, but shall not have the power or authority to award punitive damages. No party shall seek punitive damages in relation to any matter under, arising out of, or in connection with or relating to this Agreement in any other forum.

(d) Each party to any arbitration shall bear its own expense in relation thereto, including but not limited to such party's attorneys' fees, if any, and the expenses and fees of the Board of Arbitration shall be paid initially one-half by each of the Company and the Investor, but then apportioned between the Company and the Investor in the same proportion as the portion of

the related claim determined by the Board of Arbitration to be payable to the injured party bears to the portion of such claim determined not to be so payable; provided, however, that each party shall bear the costs incurred in connection with any dispute brought by such party that the Board of Arbitration determines to have been brought in bad faith.

(e) Except as provided in the last sentence of Section 11.01, the provisions of this Article XI shall be a complete defense to any suit, action or proceeding instituted in any federal, state or local court or before any administrative tribunal with respect to any dispute arising with regard to this Agreement. Any party commencing a lawsuit in violation of this Article XI shall pay the costs of the other party, including, without limitation, reasonable attorney's fees and defense costs.

## ARTICLE XII

### MISCELLANEOUS

Section 12.01. Fees and Expenses. The Company shall be solely responsible for (i) all reasonable attorneys fees and expenses incurred by the Investor in connection with the preparation, negotiation, execution and delivery of this Agreement, the Registration Rights Agreement and the Warrant up to an aggregate maximum of \$40,000, (ii) all reasonable fees and expenses incurred by the Investor in connection with any amendments, modifications or waivers of this Agreement or incurred in connection with the Investor's enforcement of this Agreement, including, without limitation, all reasonable attorneys fees and expenses, (iii) all reasonable due diligence expenses incurred by the Investor during the term of this Agreement up to aggregate maximum amount of \$7,500 per calendar quarter; provided, however, that the payments set forth in this clause (iii) shall not apply if the Company sells shares of Common Stock to the Investor with an aggregate purchase price equal to at least \$10,000,000; provided, further, that upon the Company selling shares of Common Stock to the Investor with an aggregate purchase price equal to at least \$10,000,000, the Investor shall promptly refund to the Company any amounts that were actually paid to the Investor prior to such date, and (iv) all stamp or other similar taxes and duties, if any, levied in connection with issuance of the Shares pursuant hereto; provided, however, that in each of the above instances the Investor shall provide customary supporting invoices or similar documentation in reasonable detail describing such expenses. The Investor shall reimburse all reasonable due diligence expenses incurred by the Company in connection with this transaction prior to the date of this Agreement.

Section 12.02. Reporting Entity for the Common Stock. The reporting entity relied upon for the determination of the trading price or trading volume of the Common Stock on any given Trading Day for the purposes of this Agreement shall be Bloomberg or any successor thereto. The written mutual consent of the Investor and the Company shall be required to employ any other reporting entity.

Section 12.03. Acknowledgement Regarding the Investor's Purchase of Shares. The Investor is acting solely in the capacity of an arm's length investor with respect to this Agreement and the transactions contemplated hereby. The Investor is not acting as a financial advisor or fiduciary of the Company (or in any similar capacity) with respect to this Agreement and the transactions

contemplated hereby and any advice given by the Investor or any of its representatives or agents in connection with this Agreement and the transactions contemplated hereby is merely incidental to the Investor's purchase of the Shares and may not be relied upon by the Company for any reason; provided, however, that the Company may rely upon the express representations and warranties given by the Investor under this Agreement.

Section 12.04. Brokerage. Each of the parties hereto represents that it has had no dealings in connection with this transaction with any finder or broker who will demand payment of any fee or commission from the other party. The Company on the one hand, and the Investor, on the other hand, agree to indemnify the other against and hold the other harmless from any and all liabilities to any Persons claiming brokerage commissions or finder's fees on account of services purported to have been rendered on behalf of the indemnifying party in connection with this Agreement or the transactions contemplated hereby.

Section 12.05. Notices. All notices, demands, requests, consents, approvals, and other communications required or permitted hereunder shall be in writing and, unless otherwise specified herein, shall be (i) personally served, (ii) deposited in the mail, registered or certified, return receipt requested, postage prepaid, (iii) delivered by reputable air courier service with charges prepaid or (iv) transmitted by hand delivery, telegram or facsimile, addressed as set forth below or to such other address as such party shall have specified most recently by written notice given in accordance herewith. Any notice or other communication required or permitted to be given hereunder shall be deemed effective (a) upon hand delivery or delivery by facsimile, with accurate confirmation generated by the transmitting facsimile machine, at the address or number designated below (if delivered on a business day during normal business hours where such notice is to be received), or the first business day following such delivery (if delivered other than on a business day during normal business hours where such notice is to be received) or (b) on the second business day following the date of mailing by express courier service, fully prepaid, addressed to such address, or upon actual receipt of such mailing, whichever shall first occur. The addresses for such communications shall be:

If to the Company:

Discovery Laboratories, Inc.  
350 South Main Street  
Suite 307  
Doylestown, Pennsylvania 18901  
Telephone: (215) 340-4699  
Facsimile: (215) 340-3940  
Attention: Chief Financial Officer and General Counsel



with a copy (which shall not constitute notice) to:

Dickstein Shapiro Morin & Oshinsky LLP  
1177 Avenue of the Americas, 41st Floor  
New York, NY 10036-2714  
Telephone: (212) 835-1400  
Facsimile: (212) 997-9880  
Attention: Ira L. Kotel

if to the Investor:

Kingsbridge Capital Limited  
c/o Kingsbridge Corporate Services Limited  
Main Street  
Kilcullen, County Kildare  
Republic of Ireland  
Telephone: 011-353-45-481-811  
Facsimile: 011-353-45-482-003  
Attention: Adam Gurney, Managing Director

with a copy (which shall not constitute notice) to:

Keith M. Andruschak, Esq.  
Clifford Chance US LLP  
31 West 52nd Street  
New York, NY 10019  
Telephone: (212) 878-8000  
Facsimile: (212) 878-8375

Either party hereto may from time to time change its address or facsimile number for notices under this Section by giving at least ten (10) days' prior written notice of such changed address or facsimile number to the other party hereto.

Section 12.06. Assignment. Neither this Agreement nor any rights of the Investor or the Company hereunder may be assigned by either party to any other Person.

Section 12.07. Amendment; No Waiver. No party shall be liable or bound to any other party in any manner by any warranties, representations or covenants except as specifically set forth in this Agreement or therein. Except as expressly provided in this Agreement, neither this Agreement nor any term hereof may be amended, waived, discharged or terminated other than by a written instrument signed by both parties hereto. The failure of the either party to insist on strict compliance with this Agreement, or to exercise any right or remedy under this Agreement, shall not constitute a waiver of any rights provided under this Agreement, nor estop the parties from thereafter demanding full and complete compliance nor prevent the parties from exercising such a right or remedy in the future.

Section 12.08. Entire Agreement. This Agreement, the Registration Rights Agreement and the Warrant set forth the entire agreement and understanding of the parties relating to the subject matter hereof and supersedes all prior and contemporaneous agreements, negotiations and understandings between the parties, both oral and written, relating to the subject matter hereof.

Section 12.09. Severability. In the event that any provision of this Agreement becomes or is declared by a court of competent jurisdiction to be illegal, unenforceable or void, this Agreement shall continue in full force and effect without said provision; provided, that such severability shall be ineffective if it materially changes the economic benefit of this Agreement to any party.

Section 12.10. Title and Subtitles. The titles and subtitles used in this Agreement are used for the convenience of reference and are not to be considered in construing or interpreting this Agreement.

Section 12.11. Counterparts. This Agreement may be executed in multiple counterparts, each of which may be executed by less than all of the parties and shall be deemed to be an original instrument which shall be enforceable against the parties actually executing such counterparts and all of which together shall constitute one and the same instrument.

Section 12.12. Choice of Law. This Agreement shall be construed under the laws of the State of New York.

Section 12.13. Specific Enforcement, Consent to Jurisdiction.

(a) The Company and the Investor acknowledge and agree that irreparable damage would occur in the event that any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the parties shall be entitled to an injunction or injunctions to prevent or cure breaches of the provisions of this Agreement and to enforce specifically the terms and provisions hereof or thereof, this being in addition to any other remedy to which any of them may be entitled by law or equity.

(b) Without prejudice to the terms, conditions and provisions of Article XI, the Company and the Investor irrevocably submits to the jurisdiction of the United States District Court and other courts of the United States sitting in the State of New York for the purposes of any suit, action or proceeding arising out of or relating to this Agreement and (ii) hereby waives, and agrees not to assert in any such suit, action or proceeding, any claim that it is not personally subject to the jurisdiction of such court, that the suit, action or proceeding is brought in an inconvenient forum or that the venue of the suit, action or proceeding is improper. Each of the Company and the Investor consents to process being served in any such suit, action or proceeding by mailing a copy thereof to such party at the address in effect for notices to it under this Agreement and agrees that such service shall constitute good and sufficient service of process and notice thereof. Nothing in this Section shall affect or limit any right to serve process in any other manner permitted by law. The prevailing party in any litigation in connection with this Agreement shall be entitled to recover from the other party all costs and expenses, including, without limitation, reasonable attorney's fees, incurred by such party in connection with any such litigation.

Section 12.14. Survival. The representations and warranties of the Company and the Investor contained in Articles IV and V and the covenants contained in Article V and Article VI shall survive the execution and delivery hereof and the Closing until the termination of this Agreement, and the agreements and covenants set forth in Article IX and Article X of this Agreement shall survive the execution and delivery hereof and the Closing hereunder.

Section 12.15. Publicity. Promptly after the execution of this Agreement, each party may issue a press release or otherwise make a public statement or announcement, including but not limited to, the (i) filing of a Current Report on Form 8-K with respect to this Agreement or the transactions contemplated hereby or the existence of this Agreement and (ii) and the filing of any agreements or other documents as attached exhibits to a form 8-K, 10-Q, 10-K or any other Form filed by the Company with the Commission with respect to this Agreement or the transactions contemplated hereby; provided, that prior to issuing any such press release, making any such public statement or announcement, the party wishing to make such release, statement or announcement consults and cooperates in good faith with the other party in order to formulate such press release, public statement or announcement in form and substance reasonably acceptable to both parties.

Section 12.16. Further Assurances. From and after the date of this Agreement, upon the request of the Investor or the Company, each of the Company and the Investor shall execute and deliver such instruments, documents and other writings as may be reasonably necessary or desirable to confirm and carry out and to effectuate fully the intent and purposes of this Agreement.

[Remainder of this page intentionally left blank]

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed by their respective authorized officer as of the date first written.

KINGSBRIDGE CAPITAL LIMITED

By: /s/ Valetine O'Donoghue

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Name: Valentine O'Donoghue  
Title: Director

DISCOVERY LABORATORIES, INC.

By: /s/ John G. Cooper

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Name: John G. Cooper  
Title: Executive Vice President and  
Chief Financial Officer

## REGISTRATION RIGHTS AGREEMENT

This REGISTRATION RIGHTS AGREEMENT (this "Agreement"), dated as of July 7, 2004 (the "Effective Date"), is by and between DISCOVERY LABORATORIES, INC. (the "Company"), and KINGSBRIDGE CAPITAL LIMITED (the "Investor").

WHEREAS, the Company and the Investor have entered into that certain Common Stock Purchase Agreement, dated as of the Effective Date hereof (the "Purchase Agreement"), pursuant to which the Company may issue to the Investor, from time to time, up to \$75 million worth of shares of Common Stock as provided for therein;

WHEREAS, pursuant to the terms of, and in partial consideration for the Investor entering into, the Purchase Agreement, the Company has issued to the Investor a warrant, exercisable from time to time within five (5) years following the six-month anniversary of the date of issuance (the "Warrant") for the purchase of an aggregate of up to 375,000 shares of Common Stock at a price specified in such Warrant;

WHEREAS, pursuant to the terms of, and in partial consideration for, the Investor's agreement to enter into the Purchase Agreement, the Company has agreed to provide the Investor with certain registration rights with respect to the Registrable Securities (as defined in the Purchase Agreement) as set forth herein;

NOW, THEREFORE, in consideration of the premises, the representations, warranties, covenants and agreements contained herein, in the Warrant and in the Purchase Agreement, and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, intending to be legally bound hereby, the parties hereto agree as follows (capitalized terms used herein and not defined herein shall have the respective meanings ascribed to them in the Purchase Agreement):

## ARTICLE I

## REGISTRATION RIGHTS

## Section 1.1. REGISTRATION STATEMENT.

(a) Filing of the Registration Statement. Upon the terms and subject to the conditions set forth in this Agreement, the Company shall file with the Commission, within forty-five (45) calendar days after the Effective Date, a registration statement on Form S-3 under the Securities Act or such other form as deemed appropriate by counsel to the Company for the registration for the resale by the Investor of the Registrable Securities (the "Registration Statement"). For purposes of this Agreement, the "Filing Date" shall refer to the date on which the Company files the Registration Statement.

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(b) Effectiveness of the Registration Statement. The Company shall use commercially reasonable efforts (i) to have the Registration Statement declared effective by the Commission as soon as reasonably practicable, but in any event no later than forty-five (45) calendar days after the Filing Date, or ninety (90) calendar days after the Filing Date in the event that the Commission reviews the Registration Statement, following the date that the Registration Statement is filed and (ii) to ensure that the Registration Statement remains in effect throughout the term of this Agreement as set forth in Section 4.2, subject to the terms and conditions of this Agreement.

(c) Regulatory Disapproval. The contemplated effective date for the Registration Statement as described in Section 1.1(b) shall be extended without default or liquidated damages hereunder or under the Purchase Agreement in the event that the Company's failure to obtain the effectiveness of the Registration Statement on a timely basis results from (i) the failure of the Investor to provide the Company with information requested by the Company and necessary to complete the Registration Statement by the Filing Date, (ii) the Commission's disapproval of the structure of the transactions contemplated by the Purchase Agreement, (iii) the Commission failing to respond within a customary time period to the filing of the Registration Statement or any post filing communications from the Company, or (iv) events or circumstances that are not in any way attributable to the Company; provided, that the Company has complied and continues to comply with its obligation to use commercially reasonable efforts to cause the Registration Statement to become effective. In the event of clause (ii) above, the parties agree to cooperate with one another in good faith to arrive at a resolution acceptable to the Commission.

(d) Failure to Maintain Effectiveness of Registration Statement. In the event the Company fails to maintain the effectiveness of the Registration Statement throughout the period set forth in Section 4.2, other than temporary suspensions as set forth in Section 1.1(e) or 2.1(n), and the Investor holds any Registrable Securities at any time during the period of such ineffectiveness (an "Ineffective Period"), the Company shall pay to the Investor in immediately available funds into an account designated by the Investor an amount (which shall in no event exceed \$2.5 million) equal to the product of (x) the total number of Registrable Securities issued to the Investor under the Purchase Agreement and owned by the Investor at any time during such Ineffective Period and (y) the result, if greater than zero, obtained by subtracting the VWAP on the Trading Day immediately following the last day of such Ineffective Period from the VWAP on the Trading Day immediately preceding the day on which any such Ineffective Period began; provided, however, that the foregoing payments shall not apply in respect of Registrable Securities that (i) are otherwise freely tradable by the Investor, including, but not limited to, under Rule 144 promulgated under the Securities Act (as such rule may be amended from time to time, "Rule 144") or (ii) the Company offers to repurchase from the Investor for a per share purchase price equal to the VWAP on the Trading Day immediately preceding the day on which any such Ineffective Period began.

(e) Deferral or Suspension During a Blackout Period. If in the good faith judgment of the Company, following consultation with legal counsel (which may be internal counsel), it would be detrimental to the Company or its stockholders for the Registration Statement to be filed or for resales of Registrable Securities to be made pursuant to the Registration Statement due to (i) the existence of a material development or potential material development involving the Company that the Company would be obligated to disclose in the Registration Statement, which disclosure would be premature or otherwise inadvisable at such time or would have a Material Adverse Effect on the Company

or its stockholders or (ii) a proposed filing of or use of an existing registration statement in connection with a Company-initiated registration of any class of its equity securities, which, in the good faith judgment of the Company, would adversely effect or require premature disclosure of the filing or use of such Company-initiated registration (notice thereof, a "Blackout Notice"), the Company shall have the right to (A) immediately defer such filing for a period of not more than sixty (60) days beyond the date on which the Registration Statement was otherwise required hereunder to be filed or (B) suspend use of the Registration Statement by the Investor for a period of not more than thirty (30) days (any such deferral or suspension period, a "Blackout Period"). The Investor acknowledges that it would be seriously detrimental to the Company and its stockholders for the Registration Statement to be filed or used, or remain in effect, during a Blackout Period and therefore essential to defer such filing, or suspend the use or the effectiveness thereof, during such Blackout Period and agrees to cease any disposition of the Registrable Securities during such Blackout Period. The Company may not utilize any of its rights under this Section 1.1(e) to defer the filing of a Registration Statement (or suspend its use or effectiveness) more than six (6) times in any twelve (12) month period. In the event that, within fifteen (15) Trading Days following any Settlement Date, the Company gives a Blackout Notice to the Investor and the VWAP on the Trading Day immediately preceding such Blackout Period ("Old VWAP") is greater than the VWAP on the first Trading Day following such Blackout Period on which the Investor may sell its Registrable Securities pursuant to an effective Registration Statement ("New VWAP"), then the Company shall pay to the Investor, by wire transfer of immediately available funds to an account designated by the Investor, the "Blackout Amount." For the purposes of this Agreement, Blackout Amount means a percentage equal to: (1) seventy-five percent (75%) if such Blackout Notice is delivered prior to the fifth (5th) Trading Day following such Settlement Date; (2) fifty percent (50%) if such Blackout Notice is delivered on or after the fifth (5th) Trading Day following such Settlement Date, but prior to the tenth (10th) Trading Day following such Settlement Date; (3) twenty-five percent (25%) if such Blackout Notice is delivered on or after the tenth (10th) Trading Day following such Settlement Date, but prior to the fifteenth (15th) Trading Day following such Settlement Date; and (4) zero percent (0%) thereafter of: the product of (i) the number of Registrable Securities purchased by the Investor pursuant to the most recent Draw Down and actually held by the Investor immediately prior to the Blackout Period and (ii) the result obtained by subtracting the New VWAP from the Old VWAP; provided, however, that (i) no Blackout Amount in respect of any Blackout Period shall exceed \$2.5 million, (ii) no Blackout Amount shall be payable under this Section 1.1(e) in the event that the Registrable Securities are eligible for resale under Rule 144 during the Blackout Period and (iii) no Blackout Amount shall be payable under this Section 1.1(e) in the event that the Company offers to repurchase from the Investor for a per share purchase price equal to the VWAP on the Trading Day immediately preceding the day on which any such Ineffective Period began.

(f) Liquidated Damages. (1) The Company and the Investor hereto acknowledge and agree that the amounts payable under Sections 1.1(d) and 1.1(e) and the Blackout Shares deliverable under Section 1.1(e) above shall constitute liquidated damages and not penalties. The parties further acknowledge that (i) the amount of loss or damages likely to be incurred by the Investor is incapable or is difficult to precisely estimate, (ii) the amounts specified in such subsections bear a reasonable proportion and are not plainly or grossly disproportionate to the probable loss likely to be incurred in connection with any failure by the Company to obtain or maintain the effectiveness of the

Registration Statement, (iii) one of the reasons for the Company and the Investor reaching an agreement as to such amounts was the uncertainty and cost of litigation regarding the question of actual damages and (iv) the Company and the Investor are sophisticated business parties and have been represented by sophisticated and able legal and financial counsel and negotiated this Agreement at arm's length.

(g) The Company and the Investor agree and acknowledge that the amounts payable under Sections 1.1(d) and 1.1(e), as applicable, constitute the Investor's sole remedy with respect to the Company's failure to maintain the effectiveness for the Registration Statement or for any deferral or suspension of the Registration Statement during a Blackout Period as discussed in such Sections. The Investor further agrees and acknowledges that assuming the payment of any amount by the Company, as set forth in such Sections, the Company's failure to maintain the effectiveness of the Registration Statement or for any deferral or suspension of the Registration Statement during a Blackout Period, as applicable, shall not constitute a material breach or default of any obligation of the Company to the Investor.

(h) Additional Registration Statements. In the event and to the extent that the Registration Statement fails to register a sufficient amount of Common Stock necessary for the Company to issue and sell to the Investor and the Investor to purchase from the Company all of the Registrable Securities to be issued, sold and purchased under the Purchase Agreement and the Warrant, the Company shall prepare and file with the Commission an additional registration statement or statements in order to effectuate the purpose of this Agreement, the Purchase Agreement and the Warrant.

## ARTICLE II

### REGISTRATION PROCEDURES

Section 2.1. FILINGS; INFORMATION. The Company shall use commercially reasonable efforts to effect the registration with respect to the sale of the Registrable Securities by the Investor in accordance with the intended methods of disposition thereof. Without limiting the foregoing, the Company in each such case will use commercially reasonable efforts to perform the following acts as expeditiously as possible, but in no event later than the deadline, if any, prescribed therefor in this Agreement:

(a) Subject to Section 1.1(e), the Company shall: (i) prepare and file with the Commission the Registration Statement; (ii) use commercially reasonable efforts to cause such filed Registration Statement to become and to remain effective (pursuant to Rule 415 under the Securities Act or otherwise); (iii) prepare and file with the Commission such amendments and supplements to the Registration Statement and the Prospectus used in connection therewith (the "Prospectus") as may be necessary to keep such Registration Statement effective for the time period prescribed by Section 4.2 and in order to effectuate the purpose of this Agreement, the Purchase Agreement and the Warrant; and (iv) comply with the provisions of the Securities Act with respect to the disposition of all securities covered by such Registration Statement during such period in accordance with the intended methods of disposition by the Investor set forth in such Registration Statement; provided, however, that the Investor shall be responsible for the delivery of the Prospectus to the Persons to whom the Investor sells the Registrable Securities, and the Investor agrees to dispose of Registrable Securities in compliance with the plan of distribution described in the Registration Statement and otherwise in compliance with applicable federal and state securities or blue sky laws and regulations.



(b) If so requested by the Investor, or if the Investor determines to engage an underwriter (other than the Investor) in connection with the offering of any Registrable Securities (an "Underwritten Offering"), a managing underwriter or underwriters, the Company shall (i) promptly incorporate in a prospectus supplement or post-effective amendment such information as the managing underwriters, if any, and the Investor agrees should be included therein and (ii) make all required filings of such prospectus supplement or post-effective amendment as soon as practicable after the Company has received notification of the matters to be incorporated in such prospectus supplement or post-effective amendment; provided, however, that the Company shall not be required to take any action pursuant to this Section 2.1(b)(ii) that would, in the opinion of counsel for the Company, violate applicable law.

(c) In the event of an Underwritten Offering: (A) the Company shall enter into such reasonable agreements and take all such other reasonable actions in connection therewith (including those reasonably requested by the managing underwriters, if any) in order to expedite or facilitate the disposition of such Registrable Securities, and in such connection, the Company shall: (i) make such representations and warranties to the Investor and the underwriters with respect to the business of the Company (including with respect to businesses or assets acquired or to be acquired by the Company), and the Registration Statement, Prospectus and documents, if any, incorporated or deemed to be incorporated by reference therein, in each case, in form, substance (subject to such exceptions as the Company may disclose) and scope as are customarily made by issuers to underwriters in underwritten offerings, and confirm such representations and warranties if and when requested; (ii) consent to indemnification provisions and procedures in the underwriting agreement no less favorable to the Investor and the underwriters than those set forth herein (or such other provisions and procedures acceptable to the Company, the Investor and the managing underwriters); and (iii) deliver such documents and certificates as may be reasonably requested by the Investor, its counsel and the managing underwriters, if any, to evidence the continued validity of their representations and warranties made pursuant to clause (i) above and to evidence compliance with any customary conditions contained in the applicable underwriting agreement, this Agreement, the Purchase Agreement or the Warrant.

(B) The Investor will enter into and perform its obligations under an underwriting agreement, in usual and customary form, including, without limitation, customary indemnification and contribution obligations, with the managing underwriter of such offering, and will take such other actions as are reasonably required in order to expedite or facilitate the disposition of the Registrable Securities, unless the Investor has notified the Company in writing of its election to exclude all of its Registrable Securities from such Registration Statement; provided, however, that the Investor shall consult with the Company prior to any such Underwritten Offering and defer such offering for a reasonable period upon the commercially reasonable request of the Company.

(C) The Investor may not participate in any underwriting distribution hereunder unless it (i) agrees to sell its Registrable Securities on the basis provided in any underwriting agreements, (ii) completes and executes all questionnaires, powers of attorney, indemnities, underwriting agreements and other documents reasonably required under the terms of such underwriting agreements and (iii) agrees to pay all underwriting discounts and commissions and other fees and expenses of investment bankers and any manager or managers of such underwriting, and legal expenses of the underwriter, applicable with respect to its Registrable Securities.

(d) As early as practical prior to filing the Registration Statement or Prospectus, or any amendment or supplement thereto (excluding amendments deemed to result from the filing of documents incorporated by reference therein), the Company shall deliver to the Investor and to counsel representing the Investor, in accordance with the notice provisions of Section 4.8, copies of the Registration Statement and the Prospectus, together with exhibits thereto, which documents will be subject to review by the Investor and such counsel, and thereafter deliver to the Investor and such counsel, in accordance with the notice provisions of Section 4.8, such number of copies of the Registration Statement, each amendment and supplement thereto (in each case including all exhibits thereto), the Prospectus (including each preliminary prospectus) and such other documents or information as the Investor or counsel may reasonably request in order to facilitate the disposition of the Registrable Securities.

(e) The Company shall deliver, in accordance with the notice provisions of Section 4.8, to the Investor such number of conformed copies of the Registration Statement and of each amendment and supplement thereto (in each case including all exhibits and documents incorporated by reference), such number of copies of the Prospectus (including each preliminary prospectus and any summary prospectus) and any other prospectus filed under Rule 424 promulgated under the Securities Act relating to the Investor's Registrable Securities, and such other documents, as such seller may reasonably request to facilitate the disposition of its Registrable Securities.

(f) After the filing of the Registration Statement, the Company shall promptly notify the Investor of any stop order issued or threatened by the Commission in connection therewith and take all commercially reasonable actions required to prevent the entry of such stop order or to remove it if entered.

(g) The Company shall use commercially reasonable efforts to (i) register or qualify the Registrable Securities under such other securities or blue sky laws and regulations of each jurisdiction in the United States as the Investor may reasonably (in light of its intended plan of distribution) request and (ii) cause the Registrable Securities to be registered with or approved by such other governmental agencies or authorities in the United States as may be necessary by virtue of the business and operations of the Company and do any and all other customary acts and things that may be reasonably necessary or advisable to enable the Investor to consummate the disposition of the Registrable Securities; provided, however, that the Company will not be required to qualify generally to do business in any jurisdiction where it would not otherwise be required to qualify but for this Section 2.1(g), subject itself to taxation in any such jurisdiction, consent or subject itself to general service of process in any such jurisdiction, change any existing business practices, benefit plans or outstanding securities or amend or otherwise modify the Charter or Bylaws.

(h) In the event of an Underwritten Offering, the Company shall enter into customary agreements and take such other actions as are reasonably required in order to expedite the disposition of such Registrable Securities.

(i) The Company shall make available to the Investor (and will deliver to Investor's counsel), (A) subject to restrictions imposed by the United States federal government or any agency or instrumentality thereof, copies of all public correspondence between the Commission and the Company concerning the Registration Statement and will also make available for inspection by the Investor and any attorney, accountant or other professional retained by the Investor (collectively, the "Inspectors"), (B) upon reasonable advance notice during normal business hours all financial and other records, pertinent corporate documents and properties of the Company (collectively, the "Records") as shall be reasonably necessary to enable them to exercise their due diligence responsibility, and cause the Company's officers and employees to supply all information reasonably requested by any Inspectors in connection with the Registration Statement; provided, however, that any such Inspectors must agree in writing for the benefit of the Company not to use or disclose any such Records except as provided in this Section 2.1(i). Any and all Records that the Company determines, in good faith, to be confidential and that it notifies the Inspectors are confidential shall be treated as confidential and not be disclosed by the Inspectors unless the disclosure or release of such Records is requested or required pursuant to oral questions, interrogatories, requests for information or documents or a subpoena or other order from a court of competent jurisdiction or other judicial or governmental process; provided, however, that prior to any disclosure or release pursuant to the immediately preceding clause, the Inspectors shall provide the Company with prompt notice of any such request or requirement so that the Company may seek an appropriate protective order or waive such Inspectors' obligation not to disclose such Records; and, provided, further, that if failing the entry of a protective order or the waiver by the Company permitting the disclosure or release of such Records, the Inspectors, upon advice of counsel, are compelled to disclose such Records, the Inspectors may disclose that portion of the Records that counsel has advised the Inspectors that the Inspectors are compelled to disclose; provided, however, that upon any such required disclosure, such Inspector shall use his or her best efforts to obtain reasonable assurances that confidential treatment will be afforded such information. The Investor agrees that information obtained by it solely as a result of such inspections (not including any information obtained from a third party who, insofar as is known to the Investor after reasonable inquiry, is not prohibited from providing such information by a contractual, legal or fiduciary obligation to the Company) shall be deemed confidential and shall not be used for any purposes other than as indicated above or by it as the basis for any market transactions in the securities of the Company or its affiliates unless and until such information is made generally available to the public. The Investor further agrees that it will, upon learning that disclosure of such Records is sought in a court of competent jurisdiction, give notice to the Company and allow the Company, at its expense but with the assistance of the relevant Inspectors, to undertake appropriate action to prevent disclosure of the Records deemed confidential.

(j) In the event of an Underwritten Offering of the resale of Registrable Securities pursuant to the Registration Statement, then to the extent required by the managing underwriters and reasonably necessary to effect a sale of Registrable Securities in accordance with prevailing business practices at the time of any such underwritten sale of Registrable Securities pursuant to a Registration Statement, the Company shall deliver to the Investor a signed counterpart, addressed to the Investor, of (1) an opinion or opinions of counsel to the Company and (2) a comfort letter or comfort letters from the Company's independent public accountants, each in customary form and covering such matters of the type customarily covered by opinions or comfort letters, as the case may be, as the Investor therefor reasonably requests.

(k) The Company shall otherwise comply with all applicable rules and regulations of the Commission, including, without limitation, compliance with applicable reporting requirements under the Exchange Act.

(l) The Company shall appoint a transfer agent and registrar for all of the Registrable Securities covered by such Registration Statement not later than the effective date of such Registration Statement.

(m) The Investor shall cooperate with the Company, as reasonably requested by the Company, in connection with the preparation and filing of any Registration Statement hereunder. The Company may require the Investor to promptly furnish in writing to the Company such information as may be required in connection with such registration including, without limitation, all such information as may be requested by the Commission or the NASD or any state securities commission and all such information regarding the Investor, the Registrable Securities held by the Investor and the intended method of disposition of the Registrable Securities. The Investor agrees to provide such information requested in connection with such registration within five (5) business days after receiving such written request and the Company shall not be responsible for any delays in obtaining or maintaining the effectiveness of the Registration Statement caused by the Investor's failure to timely provide such information.

(n) Upon receipt of a Blackout Notice from the Company, the Investor shall immediately discontinue disposition of Registrable Securities pursuant to the Registration Statement covering such Registrable Securities until (i) the Company advises the Investor that the Blackout Period has terminated and (ii) the Investor receives copies of a supplemented or amended prospectus, if necessary. If so directed by the Company, the Investor will deliver to the Company (at the expense of the Company) or destroy (and deliver to the Company a certificate of destruction) all copies in the Investor's possession (other than a limited number of file copies) of the prospectus covering such Registrable Securities that is current at the time of receipt of such notice.

(o) If the Investor determines to engage in an Underwritten Offering, the Investor will enter into and perform its obligations under an underwriting agreement, in usual and customary form, including, without limitation, customary indemnification and contribution obligations, with the managing underwriter of such offering, and will take such other actions as are reasonably required in order to expedite or facilitate the disposition of the Registrable Securities. The Investor shall consult with the Company prior to any Underwritten Offering and shall defer such Underwritten Offering for a reasonable period upon the commercially reasonable request of the Company.

(o) The Investor shall not take any action with respect to any distribution deemed to be made pursuant to the Registration Statement, which would constitute a violation of Regulation M under the Exchange Act or any other applicable rule, regulation or law.

Section 2.2. REGISTRATION EXPENSES. The Company shall pay all registration expenses incurred in connection with the Registration Statement (the "Registration Expenses"), including, without limitation: (i) all registration, filing, securities exchange listing and fees required by the NASD; (ii) all registration, filing, qualification and other fees and expenses of compliance with applicable state securities or blue sky laws and regulations (including reasonable fees and disbursements of counsel in connection with blue sky qualifications of the Registrable Securities); (iii) all word processing, duplicating, printing, messenger and delivery expenses; (iv) the Company's internal expenses (including, without limitation, all salaries and expenses of its officers and employees performing legal or accounting duties); (v) the fees and expenses incurred by the Company in connection with the listing of the Registrable Securities; (vi) reasonable fees and disbursements of counsel for the Company and customary fees and expenses for independent certified public accountants retained by the Company (including the expenses of any special audits or comfort letters or costs associated with the delivery by independent certified public accountants of such special audit(s) or comfort letter(s) requested pursuant to Section 2.1(k) hereof); (vii) the fees and expenses of any special experts retained by the Company in connection with such registration and amendments and supplements to the Registration Statement and Prospectus; (viii) all reasonable fees and expenses of counsel for the Investor to the extent incurred in connection with the review, and assistance in preparation, of the Registration Statement, correspondence with the Commission and amendments and supplements to the Registration Statement and Prospectus (but only to the extent such activities were conducted at the request of the Company or its counsel); (ix) ongoing due diligence expenses of the Investor equal to \$7,500 per calendar quarter payable on the last day of each calendar quarter during the term of this Agreement; provided, however, that the payments set forth in this clause (ix) shall no longer apply for calendar quarters ending after the Company has issued and sold shares of Common Stock to the Investor for an aggregate in Draw Down Amounts equal to or greater than \$10,000,000; and (x) premiums and other costs of the Company for policies of insurance against liabilities arising out of any public offering of the Registrable Securities being registered. Any fees and disbursements of underwriters, broker-dealers or investment bankers, including without limitation underwriting fees, discounts, transfer taxes or commissions, and any other fees or expenses, including legal fees and expenses (other than those described above) if any, attributable to the sale of Registrable Securities, shall be payable by the Investor.

### ARTICLE III

#### INDEMNIFICATION

Section 3.1. INDEMNIFICATION BY THE COMPANY. The Company agrees to indemnify and hold harmless the Investor, its partners, affiliates, officers, directors, employees and duly authorized agents, and each Person or entity, if any, who controls the Investor within the meaning of Section 15 of the Securities Act or Section 20 of the Exchange Act (collectively, the "Controlling Persons"), from and against any Damages, joint or several, and any action or proceeding in respect thereof to which the Investor, its partners, affiliates, officers, directors, employees and duly authorized agents, and any Controlling Person, may become subject under the Securities Act or otherwise, as incurred, insofar as such Damages (or actions or proceedings in respect thereof) arise out of, or are based upon (i) any untrue statement or alleged untrue statement of a material fact contained in any Registration Statement, or in any preliminary prospectus, final prospectus, summary prospectus, amendment or supplement relating to the Registrable Securities or (ii) any omission or alleged omission to state therein

a material fact required to be stated therein or necessary to make the statements therein under the circumstances not misleading, and shall reimburse the Investor, its partners, affiliates, officers, directors, employees and duly authorized agents, and each such Controlling Person, for any legal and other expenses reasonably incurred by the Investor, its partners, affiliates, officers, directors, employees and duly authorized agents, or any such Controlling Person, as incurred, in investigating or defending or preparing to defend against any such Damages or actions or proceedings; provided, however, that the Company shall not be liable to the extent that any such Damages arise out of the Investor's (or any other indemnified Person's) failure to send or give a copy of the final prospectus or supplement (as then amended or supplemented) to the persons asserting an untrue statement or alleged untrue statement or omission or alleged omission at or prior to the written confirmation of the sale of Registrable Securities to such person if such statement or omission was corrected in such final prospectus or supplement; provided, further, that the Company shall not be liable to the extent that any such Damages arise out of or are based upon an untrue statement or alleged untrue statement or omission or alleged omission made in such Registration Statement, or any such preliminary prospectus, final prospectus, summary prospectus, amendment or supplement in reliance upon and in conformity with written information furnished to the Company by or on behalf of the Investor or any other person who participates as an underwriter in the offering or sale of such securities, in either case, specifically stating that it is for use in the preparation thereof. In connection with any Registration Statement with respect to which the Investor is participating, such Investor will indemnify and hold harmless, to the same extent and in the same manner as set forth in the preceding paragraph, the Company, each of its directors, officers, each Person, if any, who controls the Company within the meaning of Section 15 of the Securities Act or Section 20 of the Exchange Act (each a "Company Indemnified Person") against any Damages to which any Company Indemnified Person may become subject under the Securities Act, the Exchange Act or otherwise, insofar as such Damages arise out of or are based upon any (a)(i) untrue statement or alleged untrue statement of a material fact contained in any Registration Statement, or in any preliminary prospectus, final prospectus, summary prospectus, amendment or supplement relating to the Registrable Securities or (ii) omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements therein under the circumstances not misleading in reliance upon and in conformity with written information furnished to the Company by the Investor or on behalf of the Investor expressly for use in connection with such Registration Statement or other document or (b) any failure by the Investor to comply with prospectus delivery requirements of the Securities Act, the Exchange Act or any other law or legal requirement applicable to sales under the Registration Statement.

Section 3.2. CONDUCT OF INDEMNIFICATION PROCEEDINGS. All claims for indemnification under Section 3.1 shall be asserted and resolved in accordance with the provisions of Section 10.02 and 10.03 of the Purchase Agreement.

Section 3.3. ADDITIONAL INDEMNIFICATION. Indemnification similar to that specified in the preceding paragraphs of this Article 3 (with appropriate modifications) shall be given by the Company with respect to any required registration or other qualification of securities under any federal or state law or regulation of any governmental authority other than the Securities Act. The provisions of this Article III shall be in addition to any other rights to indemnification, contribution or other remedies which an Indemnified Party or a Company Indemnified Person may have pursuant to law, equity, contract or otherwise.

Section 3.4. CONTRIBUTION. To the extent that any indemnification provided for herein is prohibited or limited by law, the indemnifying party will make the maximum contribution with respect to any amounts for which it would otherwise be liable under this Article III to the fullest extent permitted by law. However, (a) no contribution will be made under circumstances where maker of such contribution would not have been required to indemnify the indemnified party under the fault standards set forth in this Article III, (b) no seller of Registrable Securities guilty of fraudulent misrepresentation (within the meaning of Section 11(f) of the Securities Act) will be entitled to contribution from any Person who is not guilty of such fraudulent misrepresentation, and (c) contribution (together with any indemnification obligations under this Agreement) by any seller of Registrable Securities will be limited in amount of proceeds received by such seller from the sale of such Registrable Securities.

#### ARTICLE IV

##### MISCELLANEOUS

Section 4.1. NO OUTSTANDING REGISTRATION RIGHTS. Except as otherwise disclosed in accordance with the Purchase Agreement or in the Commission Documents, the Company represents and warrants to the Investor that there is not in effect on the date hereof any agreement by the Company pursuant to which any holders of securities of the Company have a right to cause the Company to register or qualify such securities under the Securities Act or any state securities or blue sky laws and regulations of any jurisdiction.

Section 4.2. TERM. The registration rights provided to the Investor hereunder, and the Company's obligation to keep the Registration Statement effective, shall terminate at the earlier of (i) such time that is two years following the termination of the Purchase Agreement, (ii) such time as all Registrable Securities have been issued and have ceased to be Registrable Securities and (iii) upon the consummation by the Company of an "Excluded Merger or Sale" (as defined in the Purchase Agreement). Notwithstanding the foregoing, paragraphs (c) and (d) of Section 1.1, Article III, Section 4.8 and Section 4.9 shall survive the termination of this Agreement.

Section 4.3. RULE 144. The Company will, at its expense, promptly take such action as the Investor may reasonably request to enable the Investor to sell Registrable Securities without registration under the Securities Act within the limitation of the exemptions provided by Rule 144 or any similar rule or regulation hereafter adopted by the Commission; provided, that the Investor may not make any such request more than once during any calendar quarter during the term of this Agreement. If at any time the Company is not required to file such reports, it will, at its expense, forthwith upon the written request of the Investor, make available adequate current public information with respect to the Company within the meaning of paragraph (c)(2) of Rule 144 or such other information as necessary to permit sales pursuant to Rule 144. Upon the request of the Investor, the Company will deliver to the Investor a written statement, signed by the Company's principal financial officer, as to whether it has complied with such requirements.

Section 4.4. CERTIFICATE. The Company will, at its expense, forthwith upon the reasonable request of the Investor but not more than once in any calendar quarter, deliver to the Investor, a certificate signed by the Company's principal financial officer, stating (a) the Company's name, address and

telephone number (including area code), (b) the Company's Internal Revenue Service identification number, (c) the Company's Commission file number, (d) the number of shares of each class of Stock outstanding as shown by the most recent report or statement published by the Company and (e) whether the Company has filed the reports required to be filed under the Exchange Act for a period of at least ninety (90) days prior to the date of such certificate and in addition has filed the most recent annual report required to be filed thereunder.

Section 4.5. AMENDMENT AND MODIFICATION. Any provision of this Agreement may be waived, provided that such waiver is set forth in a writing executed by both parties to this Agreement. The provisions of this Agreement, including the provisions of this sentence, may not be amended, modified or supplemented, and waivers or consents to departures from the provisions hereof may not be given, unless the Company has obtained the written consent of the Investor. No course of dealing between or among any Person having any interest in this Agreement will be deemed effective to modify, amend or discharge any part of this Agreement or any rights or obligations of any person under or by reason of this Agreement.

Section 4.6. SUCCESSORS AND ASSIGNS; ENTIRE AGREEMENT. This Agreement and all of the provisions hereof shall be binding upon and inure to the benefit of the parties hereto and their respective successors and assigns. The Investor may assign its rights under this Agreement to any subsequent holder of the Registrable Securities (unless sold pursuant to an effective registration statement or in accordance with Rule 144 under the Securities Act), provided that the Company shall have the right to require any holder of Registrable Securities to execute a counterpart of this Agreement as a condition to such holder's claim to any rights hereunder. The Company may assign this Agreement at any time in connection with a sale or acquisition of the Company, whether by merger, consolidation, sale of all or substantially all of the Company's assets or similar transaction, without the consent of the Investor or other subsequent holders of Registrable Securities; provided, that the successor or acquiring Person or entity agrees in writing to assume all of the Company's rights and obligations under this Agreement. This Agreement, together with the Purchase Agreement and the Warrant sets forth the entire agreement and understanding between the parties as to the subject matter hereof and merges and supersedes all prior discussions, agreements and understandings of any and every nature among them.

Section 4.7. SEVERABILITY. In the event that any provision of this Agreement becomes, or is declared by a court of competent jurisdiction to be, illegal, unenforceable or void, this Agreement shall continue in full force and effect without said provision; provided, that such severability shall be ineffective if it materially changes the economic benefit of this Agreement to any party hereto.

Section 4.8. NOTICES. All notices, demands, requests, consents, approvals and other communications required or permitted hereunder shall be given in accordance with Section 12.04 of the Purchase Agreement.

Section 4.9. GOVERNING LAW; DISPUTE RESOLUTION. This Agreement shall be construed under the laws of the State of New York. Any dispute arising out of or relating to this Agreement shall be resolved by means of arbitration pursuant to the provisions of Article XI of the Purchase Agreement.



Section 4.10. SPECIFIC ENFORCEMENT, CONSENT TO JURISDICTION. (a) The Company and the Investor acknowledge and agree that irreparable damage would occur in the event that any of the provisions of this Agreement were not performed in accordance with their specific terms or were otherwise breached. It is accordingly agreed that the parties shall be entitled to an injunction or injunctions to prevent or cure breaches of the provisions of this Agreement and to enforce specifically the terms and provisions hereof or thereof, this being in addition to any other remedy to which any of them may be entitled by law or equity.

(b) The Company and the Investor irrevocably submit to the jurisdiction of the United States District Court and other courts of the United States sitting in the State of New York for the purposes of any suit, action or proceeding arising out of or relating to this Agreement and (ii) hereby waive, and agree not to assert in any such suit, action or proceeding, any claim that it is not personally subject to the jurisdiction of such court, that the suit, action or proceeding is brought in an inconvenient forum or that the venue of the suit, action or proceeding is improper. Each of the Company and the Investor consents to process being served in any such suit, action or proceeding by mailing a copy thereof to such party at the address in effect for notices to it under this Agreement and agrees that such service shall constitute good and sufficient service of process and notice thereof. Nothing in this Section shall affect or limit any right to serve process in any other manner permitted by law. The prevailing party in any litigation in connection with this Agreement shall be entitled to recover from the other party all costs and expenses, including, without limitation, reasonable attorney's fees, incurred by such party in connection with any such litigation.

Section 4.11 HEADINGS. The headings in this Agreement are for convenience of reference only and shall not constitute a part of this Agreement, nor shall they affect their meaning, construction or effect.

Section 4.12. COUNTERPARTS. This Agreement may be executed in multiple counterparts, each of which shall be deemed to be an original instrument and all of which together shall constitute one and the same instrument.

Section 4.13. FURTHER ASSURANCES. Each party shall cooperate and take such action as may be reasonably requested by another party in order to carry out the provisions and purposes of this Agreement and the transactions contemplated hereby.

Section 4.14. ABSENCE OF PRESUMPTION. This Agreement shall be construed without regard to any presumption or rule requiring construction or interpretation against the party drafting or causing any instrument to be drafted.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed by the undersigned, thereunto duly authorized, as of the date first set forth above.

KINGSBRIDGE CAPITAL LIMITED

By: /s/ Valetine O'Donoghue

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Name: Valentine O'Donoghue  
Title: Director

DISCOVERY LABORATORIES, INC.

By: /s/ John G. Cooper

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Name: John G. Cooper  
Title: Executive Vice President and  
Chief Financial Officer

DISCOVERY LABORATORIES SECURES \$75 MILLION COMMITTED EQUITY FINANCING  
FACILITY

Management will discuss additional details during conference call on July  
9th at 10:30 AM EDT - see details below

DOYLESTOWN, PA -- JULY 8, 2004 -- DISCOVERY LABORATORIES, INC. (NASDAQ: DSCO), has entered into a Committed Equity Financing Facility Agreement (CEFF) with Kingsbridge Capital Limited in which Kingsbridge has committed to finance up to \$75 million of capital to support Discovery's future growth. The Agreement requires Kingsbridge to purchase newly-issued shares of Discovery common stock. Discovery will ultimately determine the exact timing, amount and price of any CEFF financings, subject to certain conditions. Kingsbridge is a private investment group, which operates as a closed fund, managing substantial assets for its principal. The CEFF allows Discovery to raise capital as required, at the time, price and in amounts deemed suitable to the Company, during a three-year period once the registration statement is filed by Discovery and declared effective by the Securities and Exchange Commission.

John G. Cooper, Executive Vice President and Chief Financial Officer of Discovery commented, "The CEFF gives us enormous flexibility to raise adequate amounts of capital when needed. Our financing strategy, particularly in light of current market conditions, does not include an immediate requirement for additional equity capital. With this innovative financing structure now in place, we have an ability to finance the Company at times when we believe the appropriate value is reflected in our stock price. Normally, such value accrues after the achievement of key milestones. In addition, I feel this CEFF offers a favorable cost of capital, with discounts and associated expenses less than those seen generally in PIPEs or secondary offerings. Discovery can still participate in traditional financing structures if we feel it is beneficial to do so. This CEFF, together with our ability to avail ourselves of other traditional financing structures, allows us to make financing decisions that we believe will be in the best interest of Discovery and its shareholders. The \$75 million available from the CEFF, coupled with our existing cash balances and amounts available under credit facilities provides the Company with over \$120 million of potential financial resources."

Adam Gurney, Managing Director of Kingsbridge, stated, "We are excited by Discovery's Surfactant Replacement Therapy pipeline, which we believe is of great medical potential. Discovery has several milestones expected to be announced in 2004 and 2005 - each potentially a significant value-creating opportunity for healthcare, Discovery and its investors. Kingsbridge is very pleased to be working with Discovery as it builds the first potential surfactant product pipeline for respiratory medicine and executes its transition to a commercial company with the potential FDA approval of Surfaxin(R) for RDS."

Certain details of the Committed Equity Financing facility are as follows:

- o For a period of three years, Discovery can access up to \$75 million dollars from Kingsbridge in exchange for newly-issued shares of Discovery's common stock. Discovery may access the capital after the SEC declares effective the registration statement to be filed by Discovery covering the resale of the shares of common stock issuable in connection with the CEFF and the shares of common stock underlying the warrant discussed below.

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- o Capital may be accessed under the CEFF in tranches of up to \$18.75 million, subject to certain conditions. Each tranche will be priced during the 15-day financing period with Discovery controlling the minimum acceptable purchase price for any shares to be issued to Kingsbridge during that time. Kingsbridge shall purchase shares of common stock pursuant to the CEFF at discounts ranging from 6% to 10% of the average market price of the common stock during the financing period, with the reduced discounts applying if the price of the common stock is equal to \$9.01 or more.

- o Discovery is not obligated to utilize any of the \$75 million available under the CEFF and there are no minimum commitment or minimum use penalties. The CEFF agreement does not contain any restrictions on Discovery's operating activities, automatic pricing resets or minimum market volume restrictions.

- o The agreement does not prohibit Discovery from conducting additional debt or equity financings, including PIPEs, shelf offerings, secondary offerings or any other fixed future-priced securities.

- o Throughout the term of the CEFF, Kingsbridge is restricted from engaging in any transaction intended to reduce its economic risk of owning shares of Discovery common stock including, without limitation, the purchase of any option or contract to sell, selling "short" or "short against the box", or otherwise entering into any other security transaction the purpose of which is to hedge its risk of ownership of the common stock.
- o In connection with the CEFF, Discovery issued a warrant to Kingsbridge to purchase up to 375,000 shares of common stock at an exercise price of \$12.0744 per share. The exercise term of the warrant is five years beginning with the 6-month anniversary of the closing date of the agreement. The warrant must be exercised for cash, except in limited circumstances.

Mr. Cooper continued, "Kingsbridge is a highly-respected investment group with an extensive network of contacts within the financial community. They have been a shareholder of Discovery for the past two years. The financial and legal terms of this financing structure is the product of substantial deal and market analysis by Discovery and Kingsbridge. Both parties feel that this process has resulted in a well thought out and innovative financing vehicle."

Discovery will be hosting a conference call on Friday, July 9th at 10:30 AM EDT. Management will provide more details on the Committed Equity Financing Facility.

The call in number is 800-665-0669. This audio webcast will be available to shareholders and interested parties through a live broadcast on the Internet at [HTTP://WWW.IRCONNECT.COM/PRIMECAST/DSCO/438/INDEX.HTML](http://www.IRCONNECT.COM/PRIMECAST/DSCO/438/INDEX.HTML) and [WWW.DISCOVERYLABS.COM](http://WWW.DISCOVERYLABS.COM). It is recommended that participants log onto one of these sites at least 15 minutes prior to the call. The Internet broadcast will be available for up to 30 days after the call at both website addresses.

The securities issuable in connection with the CEFF and upon the exercise of the warrant issued to Kingsbridge have not been registered under the Securities Act of 1933 and may not be offered or sold in the United States absent registration. Discovery has agreed to file, no later than August 23, 2004, a registration statement for the resale of the shares of common stock issuable in connection with the CEFF and the shares of common stock underlying the warrant.

#### ABOUT DISCOVERY LABORATORIES

Discovery Laboratories, Inc. is a biopharmaceutical company developing its proprietary surfactant technology as Surfactant Replacement Therapies for respiratory diseases. Surfactants are compositions produced naturally in the lungs and essential for breathing. Discovery's technology produces an engineered version of natural human lung surfactant that is designed to closely mimic the essential properties of human lung surfactant. Discovery believes that through its technology, pulmonary surfactants have the potential, for the first time, to be developed into a series of respiratory therapies for critical care and other hospitalized patients where there are few or no approved therapies available.

Discovery has filed a New Drug Application with the FDA for clearance to market Surfaxin, the Company's lead product, for the prevention of Respiratory Distress Syndrome in premature infants. Discovery is currently conducting a Phase 2 clinical trial for Acute Respiratory Distress Syndrome in adults, Phase 3 and Phase 2 clinical trials for Meconium Aspiration Syndrome in full-term infants. With aerosolized surfactant formulations, Discovery is preparing to initiate a Phase 2 trial for asthma (development name DSC-104) and a Phase 2 trial for Respiratory Dysfunction in premature infants.

More information about Discovery is available on the Company's Web site at [www.DiscoveryLabs.com](http://www.DiscoveryLabs.com).

To the extent that statements in this press release are not strictly historical, including statements as to business strategy, outlook, objectives, future milestones, plans, intentions, goals, future financial conditions, future collaboration agreements, the success of the Company's product development, events conditioned on stockholder or other approval, or otherwise as to future events, such statements are forward-looking, and are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The forward-looking statements contained in this release are subject to certain risks and uncertainties that could cause actual results to differ materially from the statements made. Among the factors which could affect the Company's actual results and could cause results to differ from those contained in the forward-looking statements contained herein are the risk that financial conditions may change, risks relating to the progress of the Company's research and development, the risk that the Company will not be able to raise additional capital or enter into additional collaboration agreements (including strategic alliances for our aerosol and Surfactant Replacement Therapies), risk of delay in the Company's preparation and filing of applications for regulatory approval, risk of delay in the FDA's or other health regulatory authorities' approval of any applications filed by the Company, risks that any such regulatory authority will not approve the marketing and sale of a drug product even after acceptance of an application filed by the Company for any such drug product, risks relating to the ability of the Company's third party contract manufacturers to provide the Company with adequate supplies of drug substance and drug products for completion of any of the Company's clinical studies, other risks relating to the lack of adequate supplies of drug substance and drug product for completion of

any of the Company's clinical studies, and risks relating to the development of competing therapies and/or technologies by other companies. Companies in the pharmaceutical and biotechnology industries have suffered significant setbacks in advanced clinical trials, even after obtaining promising earlier trial results. Data obtained from tests are susceptible to varying interpretations, which may delay, limit or prevent regulatory approval. Those associated risks and others are further described in the Company's filings with the Securities and Exchange Commission including the most recent reports on Forms 10-K, 10-Q and 8-K, and any amendments thereto.

COMPANY CONTACTS:

John G. Cooper, EVP and CFO  
Kori Beer, IR & Communications  
215-340-4699