

15-May-2007

Quarterly Report

ITEM 2 -- MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

RESULTS OF OPERATIONS

The Company wound down and ceased its previous contract manufacturing operations at the end of 2004. Because of this, the past and future financial results related to contract manufacturing have been treated as discontinued operations for financial reporting purposes. Continuing operations consist of the Company's current structure as an intellectual property licensing and holding company. There were no costs involved for discontinued operations for the first quarter ended March 31, 2007 or 2006.

COMPARISON OF THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006

RESULTS OF OPERATIONS

The Company did not record any royalty income during the first quarter ended March 31, 2007, compared to royalty income of \$92,277 for the same quarter of 2006. The decrease is attributable to the previously discussed product recall by Novartis, (See Note 5 of Notes to Condensed Financial Statements in this Form 10-QSB).

Operating expenses decreased \$26,152, to \$129,202 for the first quarter ended March 31, 2007, from operating expenses of \$155,354 for the comparable quarter in 2006. The reduction in operating expenses resulted from reductions in net lease expenses, legal and accounting costs, and general overall reductions in operating expenses. The Company anticipates that it can further reduce operating expenses. However, these savings may be offset with costs related to actions the Company decides to take with respect to protection of its intellectual property.

The Company recorded a net loss from operations of \$(114,326), or \$(0.03) per basic and diluted share, for the first quarter of 2007, compared to a net loss from operations of \$(51,573), or \$(0.01) per basic and diluted share, for the first quarter of 2006. The increase in net loss from operations for the first quarter of 2007 compared to the same quarter of 2006 was primarily due to the lack of royalty income for the first quarter of 2007, and partially offset by a reduction in general operating expenses.

INCOME TAXES

The provision for income tax benefits for the first quarter of 2007 and 2006 was offset principally by a valuation allowance for deferred taxes. No federal or state income tax benefit was provided for the first quarter of 2007 and 2006, as the realization of such benefits is not reasonably assured.

EFFECT OF INFLATION

Inflation has not had a significant impact on the Company's operations or cash flow.

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents decreased \$53,394 during the first quarter ended March 31, 2007, to \$1,228,391, from cash and cash equivalents of \$1,281,785 at December 31, 2006. The decrease in cash and cash equivalents during the first quarter of 2007 from the end of 2006, was due to the lack of royalty income from Novartis relating to the previously discussed product recall, in conjunction with the reduction in cash resulting from the general outflow of operating expenses.

During the first quarter ended March 31, 2007, the Company did not collect any royalty cash under the Agreement, compared to the collection of royalty cash of \$217,793 during the comparable quarter of 2006. There were no material commitments for capital expenditures at March 31, 2007 or 2006.

The Company had working capital of \$1,033,412 and a current ratio of 5.10% at March 31, 2007 compared to working capital of \$1,130,196 and a current ratio of 6.19% at December 31, 2006. The decline in working capital and the current ratio for the first quarter of 2007 compared to December 31, 2006, was primarily due to the net loss of (\$114,326) that the Company incurred during the first quarter ended March 31, 2007, and partially offset by the exercise of stock options.

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Shareholders' equity decreased \$112,776, to \$1,184,007 at March 31, 2007 from \$1,296,783 at December 31, 2006, primarily due to the net loss the Company incurred during the first quarter ended March 31, 2007.

The Company believes its existing cash and cash equivalents will be sufficient to fund operations through 2007 based upon its current cash on hand, and the anticipated operating expenses the Company is likely to incur during 2007. The Company earns interest on its available cash. Interest income earned was \$14,876 (4.9% average annual interest) and \$11,504 (3.8% average annual interest) for the quarters ended March 31, 2007 and 2006, respectively. Management has also been proactive to rejuvenate its revenue stream from Novartis or other sources in order for the Company to be viable in the future. Management has been working with Novartis to address the issues surrounding the product recall as well as exploring other licensing opportunities pertaining to the intellectual property the Company owns.

The Company's strategy is to pursue additional agreements with Novartis and concurrently pursue similar agreements with other domestic and foreign manufacturers to enable them to use the Company's proprietary patch technology in producing or selling topical patch products in the future. Furthermore, the Company is assessing the value of its patent portfolio to enhance its options with respect to future licensing opportunities, attraction of potential merger or acquisition candidates, or the sale of the Company or public shell as a whole. The Company is also taking steps to strengthen its primary patents for territories of use, including Europe and other countries. This effort is also intended to strengthen the Company's position with respect to other Company's that may be infringing on the patents the Company owns. It is currently management's intent to fund operations with royalty income from licensing agreements or from other income derived from protection of rights pertaining to the Company's intellectual property.

The Company has recently been granted a re-examination certificate which expands the Company's prior claims for a major patent the Company holds. This will enhance and strengthen the Company's position with respect to potential patent infringement in the marketplace. The Company is taking steps to evaluate its current position in light of this event.

The Company's working capital requirements are dependent upon adequate levels of royalty and licensing income to fund operations. Royalty income is uncertain because it is subject to factors that the Company cannot control. There can be no assurance that the anticipated revenue stream or the anticipated expenses will be as planned, or that the Company will be successful in negotiating other licensing opportunities with Novartis or other companies, due to the uncertainties and risks described in the "Cautionary Statements" included as Exhibit 99.01 to the Company's annual report on Form 10-KSB for the fiscal year ended December 31, 2006.

CRITICAL ACCOUNTING POLICIES

Management believes that the Company has not adopted any critical accounting policies which, if changed, would result in a material change in financial estimates, financial condition, results of operation or cash flows for the three months ended March 31, 2007 and 2006. The critical accounting policies appear in Note 2 of Notes to Condensed Financial Statements in this Form 10-QSB.

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Reference:

<http://biz.yahoo.com/e/070515/lect.ob10qsb.html>