INTERPHARM HOLDINGS INC
Form PRER14C
January 16, 2008

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

SCHEDULE 14C
INFORMATION STATEMENT PURSUANT TO SECTION 14(c)
OF THE SECURITIES EXCHANGE ACT OF 1934

Check the appropriate box:
x Preliminary Information Statement
o Confidential, for Use of the Commission Only (as permitted by Rule 14(c)-5(d)(2))
o Definitive Information Statement

INTERPHARM HOLDINGS, INC.
(Name of the Registrant as Specified in its Charter)

Payment of Filing Fee (Check the appropriate box):
x No Fee Required
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1. Title of each class of securities to which transaction applies:

2. Aggregate number of securities to which transaction applies:

3. Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

4. Proposed aggregate value of transaction:

5. Total fee paid:

o Fee paid previously with preliminary materials.
o Check box is any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

1. Amount previously paid:

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4. Date filed:

INFORMATION STATEMENT

January 15, 2008

INTERPHARM HOLDINGS, INC.

This Information Statement is being distributed pursuant to Rule 14c-2 of the Securities Exchange Act of 1934, as amended (the "Exchange Act") to the holders of record at the close of business on December 21, 2007 (the "Record Date") of the common stock, par value $.01 per share ("Common Stock"), of Interpharm Holdings, Inc., a Delaware corporation (the "Company"), as well as the holders of record on the Record Date of the following series of the Company's Preferred Stock: the Series B-1 Convertible Preferred Stock, par value $.01 per share ("Series B-1 Preferred Stock"); the Series C-1 Convertible Preferred Stock, par value $.01 per share (the "Series C-1 Preferred Stock"); and the Series C Convertible Preferred Stock, par value $.01 per share (the "Series C Preferred Stock").

SUMMARY

This Information Statement informs our stockholders of actions taken and approved on November 6, 2007, by the holders of our voting stock holding shares entitling such holders to cast more than a majority of the votes entitled to be cast with respect to such actions. Those actions approved the following transactions (collectively, the "Financing Transactions") accomplished pursuant to (i) a Securities Purchase Agreement dated as of November 14, 2007, by and among the Company, its wholly owned subsidiary, Interpharm, Inc., and the Purchasers identified therein (the "Securities Purchase Agreement"), and (ii) a Consent and Waiver Agreement dated as of November 7, 2007 (the "Consent and Waiver"), among the Company, Tullis-Dickerson Capital Focus III, L.P. ("Tullis"), Aisling Capital II, L.P. ("Aisling"), Cameron Reid ("Reid") and members of, and entities controlled by, the Sutaria family (who collectively control approximately 69% of our voting stock) (such members and entities being sometimes also referred to as the "Majority Shareholders"). The Financing Transactions consist of :

(i) the sale on November 7, 2007 to Maganlal and Vimla Sutaria of the Company's $3,000,000 principal amount of the Company's Junior Subordinated Secured 12% Note Due 2010 (the "Sutaria Note");

(ii) the sale on November 14, 2007 to Tullis, Aisling, Reid and Sutaria Family Realty, LLC ("SFR") of $5,000,000 principal amount of the Company's Secured 12% Notes Due 2009 (the "STAR Notes");

(iii) the exchange on November 14, 2007, of outstanding warrants to purchase an aggregate of 4,563,828 shares of our Common Stock at an exercise price of $1.639 per share that had been issued to each of Tullis and Aisling in connection with the Series B-1 Preferred Stock (the "B-1 Warrants") and the Series C-1 Preferred Stock (the "C-1 Warrants"), for amended and restated warrants entitling each of Tullis and Aisling to purchase 2,281,914 shares of Common Stock at an exercise price of $0.95 per share (the "Amended and Restated Warrants") (this transaction also being sometimes referred to as the "Warrant Exchange"); and

(iv) our agreement, upon the filing and dissemination of a definitive Information Statement on Schedule 14C (the "Stockholder Approval"), to:

- amend the Company's Certificate of Incorporation so as to (a) designate 20,825 shares of our authorized preferred stock as Series D-1 Convertible Preferred Stock, which will be convertible into shares of Common Stock at a conversion price of $0.95 per share (the "Series D-1 Preferred Shares"), and (b) reduce the conversion price of the Series B-1 Preferred Stock and the Series C-1 Preferred Stock from $1.5338 per share to $0.95 per share (the "Charter Amendments");
- exchange the STAR Notes for (a) the Company's Secured Convertible 12% Notes Due 2010 (the "Convertible Notes") in an aggregate principal amount equal to the principal amount of the STAR Notes plus accrued interest thereon through the date of such exchange, which will be convertible into shares of Common Stock at a conversion price of $0.95 per share, and (b) 5-year warrants (the "New Warrants") to purchase an aggregate of 1,842,103 shares of Common Stock at an exercise price of $0.95 per share (this transaction also being sometimes referred to as the "STAR Note Exchange"); and
- exchange all of the outstanding shares of the Series B-1 Preferred Stock and the Series C-1 Preferred Stock (all of which are owned by Tullis and Aisling) for the Series D-1 Preferred Shares (this transaction also being sometimes referred to as the "Preferred Stock Exchange").

A copy of the Written Consent of a Majority of the Shareholders approving the foregoing actions is attached to this Information Statement as Exhibit A.

The Charter Amendments will not become effective, and the re-pricing of the Series B-1 and C-1 Preferred Stock and the Preferred Stock Exchange will not occur, until the filing with the Office of the Secretary of State of Delaware of a Certificate of Designations, Preferences and Rights of the Series D-1 Preferred Shares at least 20 days after the date of the mailing of this Information Statement to the Company's stockholders. Similarly, the STAR Note Exchange will not occur until at least 20 days after the date of the mailing of this Information Statement to our stockholders.

This Information Statement is being disseminated to our stockholders on or about January 15, 2008.

THIS IS NOT A NOTICE OF A SPECIAL MEETING OF STOCKHOLDERS AND NO STOCKHOLDER MEETING WILL BE HELD TO CONSIDER ANY MATTER DESCRIBED HEREIN. WE ARE NOT ASKING YOU FOR A PROXY AND YOU ARE REQUESTED NOT TO SEND US A PROXY.

RECORD DATE; OUTSTANDING SHARES; VOTES APPROVING THE FINANCING TRANSACTIONS

As of the Record Date, December 21, 2007, the number of shares of each class of the Company's voting stock outstanding was as follows:

- 66,190,053 shares of Common Stock,
- 10,000 shares of Series B-1 Preferred Stock,
- 10,000 shares of Series C-1 Preferred Stock, and
- 276,747 shares of Series C Preferred Stock.

Each share of our Common Stock and Series C Preferred Stock is entitled to one vote on all matters, and vote together as a single class. Each share of our Series B-1 Preferred Stock and our Series C-1 Preferred Stock is, subject to certain limitations, entitled to that number of votes as is equal to the number of shares of Common Stock such preferred share is convertible into at the Record Date and votes together with all other classes of our stock as a single class, except that the Certificate of Designations, Preferences and Rights of each of the Series B-1 Preferred Stock and the Series C-1 Preferred Stock provides that the approval of the holders of at least a majority of the outstanding shares of Series B-1 Preferred Stock and/or (as the case may be) the Series C-1 Preferred Stock, voting as a separate class, is necessary to, among other things, amend or repeal any provision of or add any provision to our Certificate of Incorporation that would materially adversely alter or change any of the powers, preferences, privileges or rights of that series of preferred stock. In addition, Section 242 of the Delaware General Corporation Law requires that the holders of the outstanding shares of a class shall be entitled to vote as a class upon a proposed amendment to the Certificate of Incorporation, if the amendment would alter or change the powers, preferences, or special rights of the shares of such class so as to affect them adversely.

On November 6, 2007, the holders of the number of shares of the class or series of the Company's stock set forth below signed written consents (see Exhibit A hereto) approving the Financing Transactions.

Class or Series	**Votes Approving The Financing Transactions** (1)	**Total Outstanding Shares of Such Class or Series**	**Percentage of Total Shares of Such Class or Series Approving the Financing Transactions**
Common Stock	46,124,780	66,190,053	69.69%(3)
Series B-1 Preferred Stock	0	10,000(2)	0%
Series C-1 Preferred Stock	0	10,000(2)	0%
Series C Preferred Stock	0	276,747	0%

(1) The holders of the Series B-1 Preferred Stock, Series C-1 Preferred Stock and Series C Preferred Stock, having had due and actual notice of the actions to be consented to, abstained from voting thereon.

(2) If the holders of the Series B-1 Preferred Stock and of the Series C-1 Preferred Stock had not abstained and, instead, had cast the votes they otherwise would have been entitled to, such holders would have been entitled to cast an aggregate of 40,000,000 votes.
(3) Calculation excludes the number of shares of Common Stock into which the Series B-1 Preferred Stock and the Series C-1 Preferred Stock were convertible on November 6, 2007.

Based on the foregoing, the requisite number of votes of the holders of each class of the Company's stock entitled to vote on the Financing Transactions, voting as separate classes as well as a single class, have been obtained.

Absence of Dissenters' Rights of Appraisal

Neither the approval of, nor the completion of, any of the Financing Transactions provides to and stockholder of the Company any right to dissent and obtain an appraisal of or payment for the stockholder's shares under the Delaware General Corporation Law or the Company's Certificate of Incorporation or By-laws.

BACKGROUND AND REASONS FOR THE FINANCING TRANSACTIONS

In February, 2006, we entered into a four-year credit and financing arrangement with the Wells Fargo Business Credit operating unit ("WFBC") of Wells Fargo Bank ("Wells Fargo") that, pursuant to a Credit and Security Agreement dated as of February 9, 2007 (the "Senior Credit Agreement"), provided the Company with a $41,500,000 credit facility (the "WFBC Credit Facility") comprised of:

- a $22,500,000 revolving credit facility;
- a $12,000,000 real estate term loan;
- a $3,500,000 machinery and equipment term loan; and
- a $3,500,000 additional/future capital expenditure facility.

Subsequent to entering into the WFBC Credit Facility arrangement, and pursuant to Securities Purchase Agreements dated May 15, 2006 and September 11, 2006 (collectively, the "2006 SPAs"), the Company received gross proceeds of $20,000,000 from the issuance and sale of the Series B-1 Preferred Stock and the Series C-1 Preferred Stock to Tullis and Aisling, respectively. In conjunction therewith, and for no additional consideration, the Company also issued the B-1 Warrants to Tullis and the C-1 Warrants to Aisling.

As of June 30, 2007, the Company had defaulted under the Senior Credit Agreement with respect to: (i) financial reporting obligations, including the submission of its annual audited financial statements for the fiscal year ended June 30, 2007, and (ii) financial covenants related to minimum cash flow requirements, maximum allowable total capital expenditures, financial leverage and unfinanced capital expenditures for the fiscal year ended June 30, 2007 (collectively, the "Existing Defaults"). At the time of the Financing Transactions, we owed approximately $26,400,000 under the WFBC Credit Facility. As a consequence, the Company was faced with the potential foreclosure of the WFBC Credit Facility, acceleration of approximately $26,400,000 of outstanding Wells Fargo indebtedness, and execution on the collateral - consisting of substantially all of the Company's property and real estate – we had pledged as security for our borrowings from Wells Fargo. If Wells Fargo had taken these actions, the Company would have suffered substantial financial losses and potential bankruptcy.

In October, 2007, WFBC agreed to waive the Existing Defaults based on the Company's consummation and receipt of $8,000,000 in fresh financing through the issuance of the subordinated debt described below, and on October 25, 2007, the Company and WFBC finalized a Forbearance Agreement that terminated on December 31, 2007 (the "Forbearance Period"), which was subsequently amended on November 13, 2007. The parties also agreed to establish financial covenants for the 2008 fiscal year prior to the conclusion of the Forbearance Period, but such agreement was not completed during the Forbearance Period.

On January 10, 2007, the Company and its wholly-owned subsidiary Interpharm, Inc. received notice (the "Notice") from Wells Fargo that they had defaulted under the Forbearance Agreement with respect to: (i) financial covenants relating to required Income Before Tax for the months ending October 31, 2007 and November 30, 2007, (ii) financial covenants relating to required Net Cash Flow for the months ending October 31, 2007 and November 30, 2007 and (iii) an obligation to have a designated financial advisor provide an opinion as to Holdings and the Company's ability to meet their fiscal year 2008 projections.

As of January 11, 2008, the Company was obligated to Wells Fargo under the Wells Fargo Agreement in the amount of $31,256,804 (the "Outstanding Amount"). The Notice states that Wells Fargo is not demanding repayment of the Outstanding Amount at this time, but that Wells Fargo reserves the right to do so.

Maganlal and Vimla Sutaria, Sutaria Family Realty, Reid (the Company's Chief Executive Officer), Tullis and Aisling offered to provide the $8,000,000 in additional, fresh financing required by Wells Fargo. Nonetheless, pursuant to the 2006 SPAs and to certain protective provisions of the Certificates of Designations, Preferences and Rights of the Series B-1 and C-1 Preferred Stock, the consent of Tullis and Aisling was required for the issuance of the Sutaria Note and for the STAR Note financing. In consideration for those consents, which are contained in the Consent and Waiver, the Company agreed to the STAR Note Exchange and the Warrant Exchange, and the Majority Shareholders agreed to give Tullis and Aisling tag along rights on certain sales by the Majority Shareholders of our Common Stock. In addition, pursuant to the Consent and Waiver, the Majority Shareholders gave a voting proxy to a committee composed of Perry Sutaria and a representative of each of Tullis and Aisling to vote their shares of Common Stock for the election of the Company's directors, and with respect to any changes in the Company's By-laws.

THE FINANCING TRANSACTIONS

On November 7, 2007, and November 14, 2007, as required by the Forbearance Agreement, the Company received a total of $8,000,000 in gross proceeds from the issuance and sale of subordinated debt, as follows:

- **Issuance of the Sutaria Note**. On November 7, 2007, Dr. Maganlal K. Sutaria, the Chairman of the Company's Board of Directors, and Vimla M. Sutaria, his wife, loaned $3,000,000 to the Company which loan is evidenced by the Sutaria Note. Interest of 12% per annum on the Sutaria Note is payable quarterly in arrears, and for the first 12 months of that Note's term may be paid in cash or, at the Company's option, in additional notes ("PIK Notes"). Thereafter, the Company is required to pay at least 8% interest in cash and the balance, at the Company's option, in cash or PIK Notes. Repayment of the Sutaria Note (and any PIK Notes issued in lieu of cash interest payments on the Sutaria Note) is secured by third priority liens on substantially all of the Company's property and real estate. Pursuant to intercreditor agreements, the Sutaria Note (and any such PIK Notes) are subordinated to the liens held by WFBC pursuant to the Senior Credit Agreement and by the holders of the STAR Notes described below. The terms of the Sutaria Note are summarized below in the section of this Information Statement entitled "**DESCRIPTION OF SECURITIES-The Sutaria Note**."

- **Issuance of the STAR Notes**. On November 14, 2007, the Company issued and sold $5,000,000 principal amount of the STAR Notes as follows:

Tullis-Dickerson Capital Focus III, L.P. ("Tullis")	$ 833,333
Aisling Capital II, L.P. ("Aisling")	$ 833,333
Cameron Reid ("Reid")	$ 833,333
Sutaria Family Realty, LLC ("SFR")	$ 2,500,000

Interest of 12% per annum on the STAR Notes is payable quarterly in arrears, and may be paid, at the Company's option, in cash or PIK Notes. Repayment of the STAR Notes (and any PIK Notes issued in lieu of cash interest payments on the STAR Notes) is secured by second priority liens on substantially all of the Company's property and real estate. As more particularly described below, the STAR Notes will be exchangeable for our Convertible Notes upon our obtaining the Stockholder Approval. The terms of the STAR Notes are summarized below in the section of this Information Statement entitled "**DESCRIPTION OF SECURITIES-The STAR Notes**."

The Company used the $8,000,000 proceeds to pay down the outstanding balance with WFBC.

Additionally, pursuant to the Securities Purchase Agreement and the Consent and Waiver, we completed (in the case of the Warrant Exchange) and agreed to consummate (in the cases of the Charter Amendments, STAR Note Exchange and Preferred Stock Exchange) the following:

- **The Warrant Exchange.** In May and September of 2006, in conjunction with issuing the Series B-1 Preferred Stock and the Series C-1 Preferred Stock to Tullis and Aisling, respectively, we also issued the B-1 Warrants to Tullis and the C-1 Warrants to Aisling. As noted above, the B-1 Warrants entitled Tullis, and the C-1 Warrants entitled Aisling, to purchase 2,281,914 shares of our Common Stock at a per share exercise price of $1.639. As part of the consideration for Tullis and Aisling entering into the Consent and Waiver with the Company, and in exchange for the B-1 and C-1 Warrants, on November 14, 2007 we issued to each of Tullis and Aisling an Amended and Restated Warrant, entitling the holder to purchase 2,281,914 shares of the Company's Common Stock at a reduced exercise price of $0.95 per share instead of $1.639 per share.

Although the aggregate number of shares of our Common Stock issuable upon the full exercise of the Amended and Restated Warrants is the same as the shares issuable upon full exercise of the B-1 Warrants and C-1 Warrants (in either case resulting in an approximately 6.8% reduction in the voting power and per share earnings of our presently outstanding Common Stock), as compared to the B-1 and C-1 Warrants, the reduced exercise price of the Amended and Restated Warrants will result in an approximately $3,000,000 (or 58%) reduction in the gross proceeds to the Company if the Amended and Restated Warrants are fully exercised. In all other respects the Amended and Restated Warrants are identical to the B-1 and C-1 Warrants.

The terms of the Amended and Restated Warrants are summarized below in the section of this Information Statement entitled “Description of Securities- **The Amended and Restated Warrants**.”

- **The Charter Amendments.** As indicated above, and in addition to the Warrant Exchange, in consideration of Tullis and Aisling entering into the Consent and Waiver (which was necessary in order for us to sell the Sutaria Note and the STAR Notes and thereby fully meet Wells Fargo’s requirement under the Forbearance Agreement that the Company raise an additional $8,000,000 in financing) the Company agreed to (a) file with the Secretary of State of Delaware a Certificate of Designations, Preferences and Rights for a new series of our preferred stock, the Series D-1 Convertible Preferred Stock, which filing will have the effect under the Delaware General Corporation Law of amending the Company’s Certificate of Incorporation, and (b) further amend the Certificate of Incorporation so as to reduce the conversion price of the Series B-1 Preferred Stock and Series C-1 Preferred Stock in each case to $0.95 per share. Pursuant to the Consent and Waiver these filings (the “Charter Filings”) shall be made no earlier than January 18, 2008, and no later than February 28, 2008 (or such later date as may be necessary to address any SEC comments with respect to this Information Statement).

The terms and provisions of the Series D-1 Preferred Stock will be substantially identical to those of the Series B-1 Preferred Stock and Series C-1 Preferred Stock, except that the conversion price of the Series D-1 Preferred Stock will be $0.95 per share instead of $1.5338 per share, and the Series D-1 Preferred Stock will have anti-dilution protection more favorable to the holders than does the Series B-1 and C-1 Preferred Stock. As more fully described below under the section of this Information Statement entitled “The Preferred Share Exchange,” the Series D-1 Preferred Stock will, pursuant to the Consent and Waiver, be issued to Tullis and Aisling in exchange for the presently outstanding Series B-1 and C-1 Preferred Stock, of which they are the sole holders. The terms of the Series D-1 Preferred Stock are summarized below in the section of this Information Statement entitled “DESCRIPTION OF SECURITIES- The Series D-1 Preferred Stock .”

- **The STAR Note Exchange.** Pursuant to the Securities Purchase Agreement, upon completing the process of obtaining the Stockholder Approval (which, pursuant to the Consent and Waiver, consists of filing with the SEC a Preliminary Information Statement on Schedule 14C relating to the Financing Transactionsand filing a Definitive Information Statement on Schedule 14C with the SEC and disseminating the same to those of our shareholders who, as of the Record Date, would have been entitled to vote on the Financing Transactions had a shareholders’ meeting been called) the STAR Notes will be exchanged for (a) the Company’s Secured Convertible 12% Notes Due 2010 (which we also have referred to as the “Convertible Notes”) in an aggregate original principal amount equal to the principal and accrued interest on the STAR Notes through the date of such exchange, and (b) the New Warrants, which will entitle the holders to purchase up to an aggregate of 1,842,103 shares of our Common Stock at an exercise price of $0.95 per share.

Initially, the Convertible Notes will be convertible into approximately 5,263,000 shares of Common Stock, and the full conversion of the Convertible Notes and the full exercise of the New Warrants would result in the issuance of approximately 7,100,000 additional shares of Common Stock and, consequently, an approximately 10.6% reduction in both the voting power of our presently outstanding Common Stock and the per share earnings (and, hence, theoretical value) of that Common Stock. Further, to the extent that the $0.95 per share conversion price of the Convertible Notes and the $0.95 exercise price of the New Warrants are less than the per share price paid for our presently outstanding Common Stock, conversion and/or exercise will be dilutive to our present shareholders. Additionally, the Convertible Notes and the New Warrants will have anti-dilution protection with respect to issuances of Common Stock or Common Stock equivalents at less than $0.95 per share ("Dilutive Shares"), pursuant to which their conversion or exercise prices will, in those cases, automatically be re-set to a price equal to 90% of the price at which the Dilutive Shares are deemed to have been issued. In the case of the Convertible Notes, such a re-set would increase the above-noted effects on the voting power and per share earnings of our presently outstanding Common Stock.

The repayment of the Convertible Notes will be secured by second priority liens on substantially all of the Company's property and real estate. Pursuant to intercreditor agreements, the Convertible Note liens will be junior in priority to those of Wells Fargo, but senior to those of the Sutaria Note.

The terms of the Convertible Notes and New Warrants are summarized below in the section of this Information Statement entitled "DESCRIPTION OF SECURITIES- **The Convertible Notes**" and "DESCRIPTION OF SECURITIES-The New Warrants".

- **The Preferred Stock Exchange.** Pursuant to the Consent and Waiver, and as consideration for Tullis and Aisling entering into that agreement, upon completing the Stockholder Approval process and filing the Charter Amendments, the Series B-1 Preferred Stock and Series C-1 Preferred Stock held by Tullis and Aisling will be exchanged for shares of our new Series D-1 Preferred Stock. The exchange will be at the rate of 1.04125 Series D-1 shares for each Series B-1 or Series C-1 share, as the case may be. The Series D-1 Preferred Stock will be substantially similar to the Series B-1 and C-1 Preferred Stock, except that (a) the conversion price of the Series D-1 Preferred Stock will be $0.95 per share instead of $1.5338 per share, and (b) the Series D-1 Preferred Stock will have anti-dilution protection with respect to issuances of Common Stock or Common Stock equivalents at less than $0.95 per share ("Dilutive Shares"), pursuant to which their conversion or exercise prices will, in those cases, automatically be re-set to a price equal to 90% of the price at which the Dilutive Shares are deemed to have been issued.

As compared to the Series B-1 and C-1 Preferred Stock, the reduced, $0.95 per share conversion price and greater than 1-for-1 exchange rate of the Series D-1 Preferred Stock will increase the number of shares of our Common Stock that may become outstanding and that (because like the Series B-1 and C-1 Preferred Stock, the holders of the Series D-1 Preferred Stock are entitled to cast that number of votes on matters submitted to the vote of our shareholders as is equal to the number of shares of Common Stock issuable upon the full conversion of the holder's Series D-1 Preferred Stock) presently may be voted, by approximately 1,900,000 shares. For this reason, the full conversion of the Series D-1 Preferred Stock to be issued in the exchange will result in an approximately 3% reduction in both the voting power of our presently outstanding Common Stock and the per share earnings (and, hence, theoretical value) of that Common Stock. Further, to the extent that the $0.95 per share conversion price of the Series D-1 Preferred Stock is less than the per share price paid for our presently outstanding Common Stock, conversion will be dilutive to our present shareholders.

The terms of the Series D-1 Preferred Stock are summarized below in the section of this Information Statement entitled "DESCRIPTION OF SECURITIES- The Series D-1 Preferred Stock."

Interest of Certain Persons in the Financing Transactions

- ***Maganlal Sutaria, M.D.***, is a member of the Company's Board of Directors and serves as our Chairman of the Board. Dr. Sutaria and his wife, Vimla Sutaria, are the purchasers of the Sutaria Note, pursuant to which they have loaned $3,000,000 to the Company as part of the Financing Transactions.
- ***Raj Sutaria,*** a son of Maganlal Sutaria and brother of Perry Sutaria, M.D., is an Executive Vice President of the Company, and a 33 1/3% equity holder of Sutaria Family Realty, LLC ("SFR"), which has purchased $2,500,000 principal amount of the STAR Notes. As such, Mr. Sutaria may be deemed to have indirectly loaned $833,333 to the Company in the Financing Transactions. As an investor in the STAR Notes, SFR will receive approximately one-half in principal amount of the Convertible Notes and one-half of the New Warrants in the STAR Note Exchange. If the Convertible Notes and New Warrants to be issued to SFR in the STAR Note Exchange were fully converted and exercised, SFR would receive approximately 3,553,000 shares of our Common Stock. To the extent of his equity interest in SFR, Raj Sutaria will be an indirect beneficiary of the STAR Note Exchange.
- ***Perry Sutaria, M.D.,*** a son of Maganlal Sutaria and brother of Raj Sutaria, was elected as a member of the Company's Board of Directors on December 18, 2007. Dr. Sutaria is the beneficial owner of 66.62% of the Company's outstanding Common Stock and is a 33 1/3% equity holder of Sutaria Family Realty, LLC ("SFR"), which has purchased $2,500,000 principal amount of the STAR Notes. As such, Dr. Sutaria may be deemed to have indirectly loaned $833,333 to the Company in the Financing Transactions. As an investor in the STAR Notes, SFR will receive approximately one-half in principal amount of the Convertible Notes and one-half of the New Warrants in the STAR Note Exchange. If the Convertible Notes and New Warrants to be issued to SFR in the STAR Note Exchange were fully converted and exercised, SFR would receive approximately 3,553,000 shares of our Common Stock. To the extent of his equity interest in SFR, Perry Sutaria will be an indirect beneficiary of the STAR Note Exchange.
- ***Joan P. Neuscheler*** is a member of the Company's Board of Directors and the President of Tullis-Dickerson Capital Focus III, L.P., which has purchased $833,333 principal amount of the STAR Notes, will receive a ratable one-sixth portion of the Convertible Notes and New Warrants in the STAR Note Exchange, and will receive one-half of the Series D-1 Preferred Stock and of the Amended and Restated Warrants. If the Convertible Notes, New Warrants, Series D-1 Preferred Stock and Amended and Restated Warrants to be issued to Tullis in the STAR Note Exchange, Warrant Exchange and Preferred Stock Exchange were fully converted and exercised, Tullis would receive approximately 14,426,000 shares of our Common Stock.

- ***Cameron Reid*** is the Company's Chief Executive Officer, the purchaser of $833,333 principal amount of the STAR Notes, and will receive a ratable one-sixth portion of the Convertible Notes and New Warrants in the STAR Note Exchange. If the Convertible Notes and New Warrants to be issued to Reid were all fully converted and exercised, Reid would receive 1,184,210 shares of our Common Stock.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth as of December 21, 2007, certain information with respect to the beneficial ownership of our voting securities by (i) any person known by us to be the beneficial owner of more than 5% of our voting securities, (ii) each director, (iii) each executive officer, and (iv) all directors and executive officers as a group.

Name and Address of Beneficial Owner	**Title of Class**	**Amount and Nature of Beneficial Ownership**	**Percent of Class** (1)
Maganlal K. Sutaria 75 Adams Avenue Hauppauge, NY 11788	Common Stock	1,243,500(2)	1.84%
Raj Holdings I, LLC(3) 75 Adams Avenue Hauppauge, NY 11788	Common Stock	15,526,100(3)	23.26%
Bhupatlal K. Sutaria 75 Adams Avenue Hauppauge, NY 11788	Common Stock	452,970(4)	*
Rametra Holdings I, LLC 75 Adams Avenue Hauppauge, NY 11788	Common Stock	8,014,930(5)	12.01%
David Reback 75 Adams Avenue Hauppauge, NY 11788	Common Stock	61,000(6)	*
Stewart Benjamin 75 Adams Avenue Hauppauge, NY 11788	Common Stock	46,000(7)	*
Ravi Holdings I, LLC 75 Adams Avenue Hauppauge, NY 11788	Common Stock	10,518,645(8)	15.76%

Perry Sutaria 75 Adams Avenue Hauppauge, NY 11788	Common Stock	44,093,769(9)	66.07%
Kennith C. Johnson 75 Adams Avenue Hauppauge, NY 11788	Common Stock	50,000(10)	*
Cameron Reid 75 Adams Avenue Hauppauge, NY 11788	Common Stock	3,175,000(11)	4.55%
P&K Holdings, LLC 75 Adams Avenue Hauppauge, NY 11788	Common Stock	8,014,928(12)	12.01%
Richard J. Miller 75 Adams Avenue Hauppauge, NY 11788	Common Stock	25,000(13)	*
Joan P. Neuscheler c/o Tullis Dickerson Co., Inc. Two Greenwich Plaza Greenwich, Connecticut 06830	Common Stock	9,458,402(14)	12.51%
Tullis Dickerson Capital Focus III, L.P. Two Greenwich Plaza Greenwich, Connecticut 06830	Common Stock	9,433,402(15)	12.48%
Aisling Capital II, L.P. 888 Seventh Avenue, 30th Floor New York, New York 10106	Common Stock	9,194,394(16)	12.11%
George Aronson 75 Adams Avenue Hauppauge, NY 11788	Common Stock	72,451	*
Peter Giallorenzo 75 Adams Avenue Hauppauge, NY 11788	Common Stock	20,000(17)	*
Kenneth Cappel 75 Adams Avenue Hauppauge, NY 11788	Common Stock	125,625(18)	*
Jeffrey Weiss 75 Adams Avenue Hauppauge, NY 11788	Common Stock	235,875(19)	*
All Directors and	Common Stock	62,050,060(20)	77.07%

Officers as a Group (15 persons)	

* Less than 1%

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(1) Computed based upon a total of 66,738,422 shares of common stock outstanding as of December 21, 2007.

(2) The foregoing figure reflects the ownership of 543,500 shares of common stock and vested options to acquire 700,000 shares. It does not include 1,874,000 shares of Series A-1 Preferred Stock held by an annuity he controls.

(3) Raj Sutaria is the sole member of Raj Holdings I, LLC, which holds 15,526,100 shares of common stock. The sole manager of Raj Holdings I, LLC is Perry Sutaria.

(4) The foregoing figure includes 452,970 shares of common stock held directly by Mr. Sutaria, but does not include 199,411 shares held by his spouse.

(5) Mona Rametra is the sole member of Rametra Holdings I, LLC, which holds 8,014,930 shares of common stock. The sole manager of Rametra Holdings I, LLC is Perry Sutaria.

(6) The foregoing figure comprises vested options to acquire 61,000 shares of common stock.

(7) The foregoing figure comprises 46,000 shares of common stock which may be acquired upon exercise of currently exercisable options.

(8) Ravi Sutaria is the sole member of Ravi Holdings I, LLC, which holds 10,518,645 shares of common stock. The sole manager of Ravi Holdings I, LLC is Perry Sutaria.

(9) Includes an aggregate of 42,074,603 shares of common stock owned directly by the following New York limited liability companies of which Perry Sutaria is the sole manager: P&K Holdings, LLC; Raj Holdings I, LLC; Ravi Holdings I, LLC; and Rametra Holdings I, LLC. Does not include his beneficial interest in Series A-1 Preferred Stock held by a trust of which he is a beneficiary. The balance of 2,019,166 shares are shares held directly by Perry Sutaria.

10) The foregoing figure comprises vested options to acquire 50,000 shares of common stock.

(11) The foregoing figure includes vested options to purchase 3,000,000 shares of common stock and 175,000 shares held directly Mr. Reid.

(12) Perry Sutaria is the sole member and manager of P&K Holdings, LLC, which holds 8,014,928 shares of common stock.

(13) The foregoing figure comprises vested options to acquire 25,000 shares of common stock.

(14) Includes all 9,433,402 shares beneficially owned by Tullis-Dickerson Capital Focus III, L.P. ("TD III") as set forth in the table. Ms. Neuscheler is a principal of TD III and shares voting and dispositive power with respect to such shares, but disclaims beneficial ownership of such shares. Also includes vested options to acquire 25,000 shares of common stock.

(15) Includes an aggregate of 6,519,755 shares of common stock issuable upon conversion of Series B-1 Stock held TD III and 2,281.914 shares of common stock issuable upon exercise of warrants held by TD III, and 631,733 shares held as payment for dividends earned. Ms. Neuscheler is a principal of TD III. Ms. Neuscheler disclaims beneficial ownership of such shares within the meaning of SEC Rule 13d-3.

(16) Includes an aggregate of 6,519,755 shares of common stock issuable upon conversion of Series B-1 Stock and 2,281,914shares of common stock issuable upon exercise of warrants and 392,725 shares held as payments for

dividends earned.

(17) The foregoing figure includes vested options to acquire 20,000 shares of common stock, but does not include options to acquire 80,000 shares of common stock which are not exercisable within 60 days.

(18) The foregoing figure includes vested options to acquire 125,625 shares of common stock, but does not include options to acquire an aggregate of 114,375 shares of common stock which are not exercisable within 60 days.

(19) The foregoing figure comprises vested options to acquire 110,875 shares of common stock and 125,000 shares acquired through a subscription agreement, but does not include options to acquire an aggregate of 149,125 shares of common stock which are not exercisable within 60 days.

(20) The foregoing figure includes vested options to acquire an aggregate of 4,973,188 shares. The foregoing also includes the shares referred to in footnotes (9) and (14).

COMPENSATION OF DIRECTORS AND EXECUTIVE OFFICERS

COMPENSATION DISCUSSION AND ANALYSIS

Introduction and Corporate Governance

Our Compensation Committee (which is referred to herein as the "Committee" or as the "Compensation Committee") oversees and administers our executive compensation programs. The Committee's complete roles and responsibilities are set forth in the written charter adopted by the Board of Directors, which can be found at *www.interpharminc.com* under "Corporate Governance." The Board of Directors selected the following four individuals to serve on the Committee in November, 2006: Richard J. Miller (Chair), Kennith Johnson, David Reback and Joan Neuscheler. All of these individuals, with the exception of Richard J. Miller, qualify as an independent director under the rules of the American Stock Exchange.

The Committee meets at regularly scheduled times during the year and on an ad hoc basis as business needs necessitate. During the fiscal year ended June 30, 2007, the Committee met for three regularly scheduled meetings and held two ad hoc meeting. As part of his duties as the Committee Chair, Mr. Miller reports on Committee actions and recommendations to the Board of Directors.

The Committee has retained Frederic W. Cook and Associates ("FW Cook") as outside advisors to the Committee. FW Cook reports directly to the Committee and provides guidance on matters including trends in executive and non-employee director compensation, the development of specific executive compensation programs and other matters as directed by the Committee. FW Cook does not provide any other services to the Company.

Executive Compensation Philosophy and Objectives

Our compensation program for the individuals named in the Summary Compensation Table (the "named executive officers") is designed and implemented based on our pay-for-performance compensation philosophy. Our compensation committee's current intent is to perform an annual strategic review of our executive officers' compensation to determine whether they provide adequate incentives and motivation and whether they adequately compensate our executive officers relative to comparable officers in other companies with which we compete for executives. We strive to adhere to this philosophy by significantly differentiating the pay and rewards of our executive officers based on their demonstrated performance and potential to contribute to the long-term success of the Company. Competing for talent in the rapidly changing and increasingly competitive pharmaceutical industry is both challenging and critical to our success. The quality of the Company's talent is a key driver of long-term stockholder value. Establishing and maintaining executives' long-term commitment to us is critical to the development of our product pipeline, as development of new products often takes three years or more, and time to market is critical to our business success.

We have established a total rewards framework that supports our compensation philosophy through the following objectives:

- to afford our executives a competitive total rewards opportunity relative to organizations with which we compete for executive talent,

- to allow us to attract and retain superior, experienced people who can perform and succeed in our fast-paced, dynamic and challenging environment,

- to support our meritocracy by ensuring that our top performers receive rewards that are substantially greater than those received by average performers at the same position level, and

- to deliver pay in a cost efficient manner that aligns employees' rewards with stockholders' long-term interests.

What is our compensation program designed to reward?

The compensation program is designed to reward superior financial, strategic and operational performance that is achieved in a manner consistent with the Company's values. Results and how the results are attained are both critically important. Our executive officers are assessed on the basis of demonstrated results relative to pre-established goals, ability to address market changes in a timely and efficient manner, as well as demonstrated competencies and behavioral attributes.

Compensation Program Elements and Pay Level Determination

What factors are considered in determining the amounts of compensation?

The Committee has formalized a review process for the determination of base salaries, annual incentive targets and payments, and long-term incentive targets and awards for all executive officers. For the year ended June 30, 2007, there were no changes in the base salary or any annual cash incentive and long-term incentive award determinations for the Chief Executive Officer.

As part of this review process, the CEO presents to the Committee individual assessments of each executive officer's performance over the prior year, as well as recommended compensation actions for each executive officer. The performance assessments for executive officers include performance relative to established goals, overall leadership effectiveness, impact across the organization and performance and impact relative to other executive officers.

Formal goal setting is critical to ensuring that our compensation program rewards each executive based on his or her success relative to the specific objectives for his or her role. All Company senior managers are subject to annual goal setting, as well as annual performance reviews. The key metrics we use to measure performance differ by individual, but can be grouped into the following categories:

- Financial — we evaluate measures of Company financial performance, including revenue growth, gross margins, operating margins and other measures such as expense management.

- Strategic — we monitor the success of our executive team in furthering the strategic success of the Company, including the development of the Company's product pipeline.

- Operational — we include operational measures in our determination of success, including our production capacity and capability, the timeliness and effectiveness of new product launches, the execution of important internal Company initiatives and customer growth and retention.

The Committee considers the totality of the information presented (including external competitiveness, the performance review, Company performance, progress towards strategic objectives and internal equity) and applies its knowledge and discretion to determine the compensation for each executive officer.

During the fiscal year ended June 30, 2007, the Company targeted its compensation at the median of its market peers, which are defined in the next section. The actual compensation level for each executive officer may be above or below median depending on factors such as Company performance, individual performance, skills/capabilities, overall impact/contribution, experience in position, “premiums” initially required to attract the executive and internal equity.

What external market peer group is used for comparison, and how is it established?

The Company’s peer group is comprised of: (1) a named set of companies for which executive compensation data from public filings is compiled and analyzed; and (2) a somewhat broader set of companies participating in benchmark compensation surveys from which executive compensation data is compiled and analyzed by our compensation advisor.

The named peer group is reviewed annually by the Committee for appropriateness, considering such factors as size (e.g., revenue and market capitalization), complexity (e.g., multiple marketed products), geographic scope of operations (e.g., domestic-only presence), etc. The named peer group for the fiscal year ended June 30, 2007 includes:

Arqule	Hi Tech Phamacal	Quigley	Caraco
Bentley Pharmaceuticals	Inspire Pharmaceutical	Saviant	Theragenics
Bradley Pharmaceuticals	Lannett	Supergen	

The compensation surveys used in analyzing our external competitiveness include data from a broader set of biotechnology and pharmaceutical companies. We believe that this broader set of companies is representative of our competitive market for executive officers. These compensation surveys provide reliable data to complement the data collected from executive compensation disclosures of our named peer group.

What is each element of compensation and why is it paid?

The Company’s executive compensation program is designed with three elements (discussed in detail below), each of which serves an important role in supporting Interpharm’s pay-for-performance philosophy and in realizing our compensation program objectives:

Element	**Role and Purpose**
BaseSalary	Provide a stable source of income that facilitates the attraction and recognition of the acquired skills and contributions of executives in the day-to-day management of our business.
Long-term Incentives	Align executive interests with those of stockholders. Promote long-term retention and stock ownership, and hold executives accountable for enhancing stockholder value. Enable the delivery of competitive compensation opportunities in a manner that balances cost efficiency with perceived value.
Benefits & Perquisites	Provide programs that promote health, wellness and financial security. Provide executive benefits and perquisites at or below market competitive levels.

While the general mix of the elements is considered in the design of our total compensation program, the Committee does not target a specific mix of pay in either its program design or in its compensation determinations. By design, our executive officers have more variability than non-executives in their compensation, to more closely tie their compensation to the Company's overall performance.

Base Salary

We pay our executive officers base salaries to provide a baseline level of compensation that is both competitive with the external market and commensurate with each employee's past performance, experience, responsibilities and skills. The Company generally targets base salaries around the median of our external market peers. In making its base salary determinations, the Committee takes into account the internal and external factors described above. Base salary increases from the fiscal year ended June 30, 2006 to the fiscal year ended June 30, 2007 for our named executive officers averaged 2% and ranged from 0% to 5%. The Company's CEO received a 0% increase in the fiscal year ended June 30, 2007.

Long-term Incentives

A long-term incentive ("LTI") opportunity has been designed for managers to foster a culture of ownership, align compensation with stockholder interests and promote long-term retention and affiliation with the organization. The Committee has determined the types of awards to be used for delivering long-term incentives. In doing so, the Committee considered the ability of each type of award to achieve key compensation objectives (such as employee retention, motivation and attraction), the needs of the business, competitive market practices, dilution and expense constraints, as well as tax and accounting implications.

For the fiscal year ended June 30, 2007, the Committee evaluated various program designs and approved a program awarding stock options for our executive officers. Stock options promote stockholder alignment and accountability and are qualified as performance-based pay under Internal Revenue Code Section 162(m). Our 2007 stock option grants vest over four years.

Tax-deductibility of Compensation

Section 162(m) of the Internal Revenue Code of 1986, as amended, limits to $1 million the amount a company may deduct for compensation paid to its CEO or any of its other four named executive officers. This limitation does not, however, apply to compensation meeting the definition of "qualifying performance-based" compensation.

Management works with the Committee to assess alternatives to preserve the deductibility under Section 162(m) of compensation payments to the extent reasonably practicable, consistent with our compensation policies and as determined to be in the best interests of the Company and its stockholders. For the fiscal year ended June 30, 2007, the Company believes that the Compensation payments will meet the requirements of Section 162(m) of the Internal Revenue Code of 1986, as amended.

Perquisites and Personal Benefits

In addition to participating in the benefit programs provided to all other employees (for example, medical, dental, vision, life and disability insurance, employee stock purchase plan), we provide certain perquisites and additional benefits to executives. These supplemental benefits and perquisites include:

Auto Allowances The Company provided annual car allowance benefits to executive officers and certain management personnel. Such reimbursement is considered taxable income to the recipients.

Mobile Telephone Allowance: The Company provided monthly mobile telephone allowance benefits to executive officers and certain management personnel. Such reimbursement is considered taxable income to the recipients.

Retirement Plans

We maintain a pre-tax savings plan covering substantially all employees, which qualifies under Section 401(k) of the Internal Revenue Code. Under the plan, eligible employees, including executive management, may contribute a portion of their pre-tax salary, subject to certain limitations. The Company contributes and matches 100% of the employee pre-tax contributions, up to 3% of the employee's compensation plus 50% of pre-tax contributions that exceed 3% of compensation, but not to exceed 5% of compensation. The Company may also make profit-sharing contributions in its discretion which would be allocated among all eligible employees, whether or not they make contributions.

Summary Compensation Table
(in thousands, except per share data)

The following table shows the compensation paid to or earned by the named executive officers during the fiscal year ended June 30, 2007.

Name and 'Principal Position	**Year**	**Salary ($)**	**Bonus ($)**	**Stock Awards ($) (1)**	**Option Awards ($) (2)**	**Non-Equity Incentive Plan Compensation ($) (3)**	**Change in Pension Value and Nonqualified Deferred Compensation Earnings ($) (4)**	**All Other Compensation ($) (5)**	**Total ($)**
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
Cameron Reid	2007	$ 300	$ -	$ -	$ -	$ -	$ -	$ 13	$ 313
Chief Executive Officer	2006	$ 297	$ -	$ -	$ -	$ -	$ -	$ -	$ 297
	2005	$ 76	$ -	$ -	$ -	$ -	$ -	$ -	$ 76
Bhupatlal Sutaria	2007	$ 275	$ -	$ -	$ -	$ -	$ -	$ 13	$ 288
President	2006	$ 271	$ -	$ -	$ -	$ -	$ -	$ 22	$ 293
	2005	$ 198	$ 15	$ -	$ -	$ -	$ -	$ 21	$ 234
Peter Giallarenzo	2007	$ 110	$ -	$ -	$ 117	$ -	$ -	$ 5	$ 232
Chief Financial Officer	2006	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
	2005	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Jeffrey Weiss	2007	$ 236	$ -	$ -	$ 15	$ -	$ -	$ 12	$ 263
Executive Vice President	2006	$ 225	$ 460	$ -	$ -	$ -	$ -	$ 25	$ 710
	2005	$ 78	$ -	$ -	$ 244	$ -	$ -	$ -	$ 322
Ken Cappel	2007	$ 250	$ -	$ -	$ 13	$ -	$ -	$ 12	$ 275
General Counsel	2006	$ 232	$ -	$ -	$ -	$ -	$ -	$ 25	$ 257
	2005	$ 118	$ -	$ -	$ 330	$ -	$ -	$ 10	$ 458
George Aronson	2007	$ 236	$ -	$ -	$ -	$ -	$ -	$ 13	$ 249
Chief Financial Officer	2006	$ 221	$ -	$ -	$ -	$ -	$ -	$ 21	$ 242
	2005	$ 148	$ 15	$ -	$ 136	$ -	$ -	$ 9	$ 308
Munish Rametra	2007	$ 250	$ -					12	262
General Counsel	2006	$ 252	$ -	$ -	$ -	$ -	$ -	$ 19	$ 271
	2005	$ 165	$ 15	$ -	$ -	$ -	$ -	$ 30	$ 210

Notes to Summary Compensation Table

(1) The amounts in column (e) reflect the dollar amounts recognized for financial statement reporting purposes in accordance with SFAS 123(R) for unvested restricted stock held by each executive officer.

(2) The amounts in column (f) reflect the dollar amounts recognized for financial statement reporting purposes in accordance with SFAS 123(R) for unvested stock options held by each executive officer. Pursuant to SEC rules, the amounts shown exclude the impact of estimated forfeitures related to service-based vesting conditions.

(3) The amounts in column (g) reflect actual cash incentives awarded to each executive officer.

(4) The amounts in column (h) represent earnings in the Company's 401(k) that were contributed by the Company. We do not maintain a pension plan or a defined benefit

plan.

(5) The amounts in column (i) reflect the amount for auto allowances.

2007 Grants of Plan-Based Awards
(in thousands, except per share data)

The following table shows additional information regarding all grants of plan-based awards made to our named executive officers for the year ended June 30, 2007.

GRANTS OF PLAN-BASED AWARDS

Name	Grant Date	Estimated Future Payouts Under Equity Incentive Plan Awards Threshold (#)	Target (#)	Maximum (#)	All Other Stock Awards: Number of Shares of Stocks or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#) (1)	Exercise or Base Price of Option Awards ($/Sh) (2)	Grant Date Fair Value of Stock and Option Awards ($)(3)
Cameron Reid	**-**	**-**	**-**	**-**	**-**	**-**	**$ -**	**$ -**
Bob Sutaria	**-**	**-**	**-**	**-**	**-**	**-**	**$ -**	**$ -**
Peter Giallarenzo	**03/20/07**	**-**	**-**	**-**	**-**	**100(4)**	**$ 1.62**	**$ 117**
Jeff Weiss	**03/20/07**	**-**	**-**	**-**	**-**	**17(5)**	**$ 1.62**	**$ 15**
Ken Cappel	**03/20/07**	**-**	**-**	**-**	**-**	**14(5)**	**$ 1.62**	**$ 13**
George Aronson	**-**	**-**	**-**	**-**	**-**	**-**	**$ -**	**$ -**

Notes to 2007 Grants of Plan-Based Awards Table

(1) Grant of non performance-based stock options.
(2) Fair Market Value of stock on the date of grant
(3) Amounts represent the full grant date fair value as determined under SFAS 123(R). The value of stock options granted is based on the grant date present value as calculated using a Black-Scholes option pricing model.
(4) Options have a ten-year term and are scheduled to vest 20% each on January 8, 2008, 2009, 2010, 2011 and 2012.
(5) Options have an approximate five-year term and are scheduled to vest 25% each on June 30, 2007, 2008, 2009 and 2010.

Outstanding Equity Awards At 2007 Fiscal Year-End
(in thousands, except per share data)

The following table summarizes the equity awards we have made to each of the named executive officers that were outstanding as of June 30, 2007.

OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

	OPTION AWARDS					STOCK AWARDS			
Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#)	Option Exercise Price ($)	Option Expiration Date	Number of Shares of Units of Stock That Have Not Vested (#)	Market Value of Shares of Units of Stock That Have Not Vested ($)	Equity Incentive Plan Awards: Number of Unearned Shares, Units of Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (#)
Cameron Reid	**3,000 1**	**-**	**-**	**$ 1.23**	**06/30/10**	**-**	**-**	**-**	**-**
Jeffrey Weiss	**60 2**	**90 3**	**-**	**$ 1.23**	**06/30/10**	**-**	**-**	**-**	**-**
	47 2	**47 3**	**-**	**$ 1.23**	**06/30/11**				
	4 2	**12 3**	**-**	**$ 1.62**	**06/30/12**				
Bhupatlal K. Sutaria	**500 4**	**200 4**	**-**	**$ 0.68**	**05/30/13**	**-**	**-**	**-**	**-**
Peter Giallarenzo	**-**	**100 5**	**-**	**$ 1.62**	**03/20/17**	**-**	**-**	**-**	**-**
Kenneth Cappel	**84 6**	**66 7**	**-**	**$ 1.23**	**06/30/10**	**-**	**-**	**-**	**-**
	38 6	**38 7**	**-**	**$ 1.23**	**06/30/11**				
	3 6	**10 7**	**-**	**$ 1.62**	**06/30/12**				
George Aronson	**-**	**-**				**-**	**-**		
Estate of Munish Rametra	**450 8**	**-**	**-**	**$ 0.68**	**03/31/09**	**-**	**-**	**-**	**-**

Notes to Outstanding Equity Awards at 2007 Fiscal Year-End Table

(1) Represents fully vested options that: (i) are exercisable at $1.23 per share through June 30, 2010 and (ii) were repriced as follows: options to purchase 2,000 shares of common stock originally granted at $2.24 per share were repriced to $1.23 per share and options to purchase 1,000 shares of common stock originally granted at $3.97 per share were repriced

to $1.23 per share at June 30, 2005.

(2) Represents 60 options that are exercisable at $1.23 per share through June 30, 2015, 47 options that are exercisable at $1.23 per share through June 30, 2011, and 4 options that are exercisable at $1.62 through June 30, 2012.

(3) Represents 90 options exercisable at $1.23 per share that have various vesting dates through June 30, 2010 and are exercisable through June 30, 2015, 47 options exercisable at $1.23 per share through June 30, 2011 and 12 options exercisable at $1.62 that have various vesting dates through June 30, 2012.

(4) Represents options that are exercisable at $0.682 per share. These options have the following vesting provisions: 25% of the options vested on January 1, 2005, December 31, 2005, and December 31, 2006, respectively and an additional 25% will vest on December 31, 2007.

(5) Represents options that are exercisable at $1.46 per share. The shares have various vesting dates through January 8, 2012 and are exercisable through March 20, 2017.

(6) Represents 84,000 fully vested repriced options that are exercisable at $1.23 per share through June 30, 2010, 38,250 options exercisable at $1.23 per share through June 30, 2011 and 3,375 options that are exercisable at $1.62 through June 30, 2012. The June 30, 2005 repriced options were originally granted at $1.94 per share.

(7) Represents (a) 104 options that are exercisable at $1.23 per share and vest 41 on June 30, 2008 and June 30, 2009, respectively, and 22 options that vest on June 30, 2010 and (b) 10 options that are exercisable at $1.62 per share and vest 3 on June 30, 2008, June 30, 2009 and 4 on June 30, 2010.

(8) Represents 450 fully vested options that are exercisable at $0.68 per share through March 31, 2009.

2007 Options Exercised and Stock Vested
(in thousands, except per share data)

The following table summarizes the options exercised and stock vested by our named executive officers during the year ended June 30, 2007.

OPTION EXERCISES AND STOCK VESTED

	OPTION AWARDS		**STOCK AWARDS**	
Name	**Number of Shares Aquired On Exercise (#)**	**Value Realized on Exercise ($)**	**Number of Shares Aquired On Vesting (#)**	**Value Realized on Vesting ($)**
Cameron Reid	-	-	-	-
Jeffrey Weiss	-	-	-	-
Bhupatlal K. Sutaria	-	-	-	-
Peter Giallarenzo	-	-	-	-
Kenneth Cappel	-	-	-	-
George Aronson	72(1)	$ 120(1)	-	-
Estate of Munish Rametra	-	-	-	-

Notes to 2007 Options Exercised and Stock Vested Table
(1) Represents cashless exercises of 302 options to purchase our common stock. Of the total amount exercised, 108 options were Incentive Stock Options resulting in the acquisition of 28 shares having a value of $47, and 194 options were Nonqualified Options resulting in the acquisition of 44 shares and having a value of $73.

2007 Pension Benefits

There were no pension benefits granted to named executive officers during the year ended June 30, 2007.

Nonqualified Deferred Compensation Plans

There were no contributions to any nonqualified defined contribution or other nonqualified deferred compensation plans for any named executive officers during the year ended June 30, 2007.

Director Compensation

Dr. Maganlal Sutaria, the only employee member of the Board of Directors, received no extra compensation for his service on the Board of Directors. Effective November 2006, a standard compensation package was adopted for all non-employee members of our Board of Directors based upon a review of similar sized companies in the pharmaceutical industry as follows:

· 15,000 fully vested stock options as of the date of appointment to the Board;
· 10,000 options as of the first day of a year served;
· An annual retainer of $10,000;
· $1,500 for each meeting day of the Board of Directors attended (in person);
· A fee of not greater than $500 for each meeting day of the Board of Directors attended (by telephone) and determined by the Compensation Committee Chairperson;
· $750 for each committee meeting attended (in person or by telephone);

In addition to the fees described above: (i) the chairs of our Audit Committee, Compensation Committee, receive an additional annual retainer of $5,000 respectively; (ii) the members of our Audit Committee (other than the chair) receive an additional annual retainer of $1,000; (iii) David Reback and Stewart Benjamin were granted 16,000 fully vested options and $10,000 for all past Board service provided; and (iv) Kennith Johnson was granted 40,000 fully vested options for past Board service provided.

The following Director Compensation Table sets forth summary information concerning the compensation paid to our non-employee directors in fiscal 2007 for services to the Company.

DIRECTOR COMPENSATION

Name	Fees Earned or Paid in Cash ($) (1)	Stock Awards ($)	Option Awards ($) (2)	Non-Equity Incentive Plan Compensation ($)	Change in Pension Value and Nonqualified Deferred Compensation Earnings ($)	All Other Compensation ($)	Total ($)
Stewart Benjamin	**$ 34**	**$ -**	**$ 25**	**$ -**	**$ -**	**$ -**	$ 59
Kennith Johnson	**$ 48**	**$ -**	**$ 49**	**$ -**	**$ -**	**$ -**	$ 97
David Reback	**$ 38**	**$ -**	**$ 25**	**$ -**	**$ -**	**$ -**	$ 63
Richard Miller	**$ 30**	**$ -**	**$ 24**	**$ -**	**$ -**	**$ 112**(3)	$ 166
Joan Neuscheler	**$ 23**	**$ -**	**$ 24**	**$ -**	**$ -**	**$ -**	$ 47

Notes to 2007 Options Exercised and Stock Vested Table

(1) Amounts represent fees paid for Board Meetings and sub-committee meetings, as well as fees for Board membership and membership in certain sub-committees.

(2) Amounts represent the full grant date fair value as determined under SFAS 123(R). The value of stock options granted is based on grant date present value as calculated using a Black-Scholes option pricing model.

(3) Amount represents monies paid to a consulting firm of which Mr. Miller is a principal.

Compensation Committee Interlocks and Insider Participation

None of the Compensation Committee members is, or was ever, an officer or employee of the Company or any of its subsidiaries, nor did any of the Compensation Committee members have any relationship requiring disclosure by the Company under any subsection of Item 404 of Regulation S-K promulgated by the SEC. During the last fiscal year, none of the executive officers of the Company served on the board of directors or on the compensation committee of any other entity, any of whose executive officers served on the Board.

Compensation Committee Report

The Compensation Committee, comprised of independent directors with the exception of Richard J. Miller, reviewed and discussed the Compensation Discussion and Analysis set forth above with the Company's management. Based on such review and discussion, the Compensation Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in the Company's Annual Report on Form 10-K for the year ended June 30, 2007 and in the proxy statement.

Compensation Committee:

Richard J. Miller (Chairman)
Kennith Johnson
Joan Neuscheler
David Reback

DESCRIPTION OF SECURITIES

The following tables set forth summary descriptions of the securities (other than our Common Stock) issued and to be issued in connection with the Financing Transactions and includes a summary of the Designations, Preferences and Rights of the Series D-1 Preferred Stock which will be filed in the Charter Amendments..

The Sutaria Note

ITEM	DESCRIPTION
Title	Junior Subordinated Secured 12% Note Due 2010
Principal Amount	$3,000,000
Interest Rate and Payment of Interest	12% per annum, payable quarterly in arrears. For the first 12 months, interest is payable in cash or additional promissory notes in a principal amount equal to the interest then due and payable ("PIK Notes"), at the Company's option. Thereafter, unless the holder otherwise consents, two-thirds of said interest (8%) shall be paid in cash, and the remaining one-third (4%) is payable in cash or PIK Notes, at the Company's option. PIK Notes accrue interest at the same rate as the Sutaria Note and are in all other respects identical to the Sutaria Note.
Payment of Principal	The outstanding principal balance, together with any then accrued but unpaid interest, is due and payable on the Maturity Date.
Maturity Date	November 7, 2010

Default Provisions	In addition to customary default provisions, the Sutaria Note provides that a default under the Wells Fargo Senior Credit Agreement constitutes a default under the Sutaria Note.
Pre-payment	The Company may, in whole or in part, pre-pay the principal amount of, plus all accrued, but unpaid interest on, the Sutaria Note at any time on 30 days' prior notice to the holder.
Security, Security Interest and Priority	The Company's obligations under the Sutaria Note are secured by a third priority security interest in and lien on substantially all of the Company's property and real estate, subordinated to the Company's obligations under the WFBC Credit Facility, and the STAR Notes and Convertible Notes.
Conversion Rights	None

The STAR Notes

ITEM	DESCRIPTION
Title	Secured 12% Notes Due 2009
Aggregate Principal Amount	$5,000,000
Interest Rate and Payment of Interest	12% per annum, payable quarterly in arrears. The STAR Notes are payable, at the Company's option, either in cash, additional promissory notes in a principal amount equal to the interest then due and payable ("PIK Notes") or, in lieu of a PIK Note, by adding the amount of such then due and payable interest to the principal amount of the STAR Note. PIK Notes accrue interest at the same rate as, and in all other respects are identical to, the STAR Notes.
Payment of Principal	The outstanding principal balance, together with any then accrued but unpaid interest, is due and payable on the Maturity Date.
Maturity Date	November 14, 2009
Default Provisions	In addition to customary default provisions, the STAR Notes provide that a default under the Wells Fargo Senior Credit Agreement also constitutes a default under the STAR Notes.
Pre-payment	The STAR Notes may not be pre-paid.
Conversion Rights	None.
Exchange for Convertible Notes and Warrants	Upon the filing with the SEC of a Definitive Information Statement on Schedule 14C relating to the Financing Transactions, which shall occur no sooner than January 18, 2008 and no later than February 28, 2008 (or such later date as may be necessary to address and clear any SEC comments regarding any Preliminary Information Statement on Schedule 14C filed by the Company, the STAR Notes shall be exchanged for (a) the Company's Secured Convertible 12% Promissory Notes Due 2010 (the "Convertible

Notes") in an aggregate original principal amount equal to the principal and accrued interest on the STAR Notes through the date of such exchange, and (b) warrants (the "New Warrants") to purchase up to an aggregate of 1,842,103 shares of our Common Stock at an exercise price of $0.95 per share. The terms of the Convertible Notes and the New Warrants are more fully summarized below in the tables entitled "The Convertible Notes" and "The New Warrants."

Security, Security Interest and Priority	The Company's obligations under the STAR Notes are secured by a second priority security interest in and lien on substantially all of the Company's property and real estate, subordinated to the Company's obligations under the WFBC Credit Facility, but senior to the Sutaria Note.

The Convertible Notes

ITEM	DESCRIPTION
Title	Secured Convertible 12% Notes Due 2010_
Aggregate Principal Amount	The aggregate principal amount of the Convertible Notes will be equal to the outstanding principal and accrued interest on the STAR Notes through the date on which they are issued in exchange for the STAR Notes.
Interest Rate and Payment of Interest	When issued, the Convertible Notes will bear interest at the rate of 12% per annum, payable quarterly in arrears. When issued, the Convertible Notes will be payable, at the Company's option, either in cash, additional promissory notes in a principal amount equal to the interest then due and payable ("PIK Notes") or, in lieu of a PIK Note, by adding the amount of such then due and payable interest to the principal amount of the Convertible Note. Such PIK Notes, when and if issued, will accrue interest at the same rate as, and in all other respects will be identical to, the Convertible Notes.
Payment of Principal	The outstanding principal balance, together with any then accrued but unpaid interest, will be due and payable on the Maturity Date.
Maturity Date	The Convertible Notes will mature 2 years from their date of issuance.
Default Provisions	In addition to customary default provisions, the Convertible Notes will provide that a default under the Wells Fargo Senior Credit Agreement will also constitute a default under the Convertible Notes.
Prepayment	The Company may, in whole or in part, pre-pay the principal amount of, plus all accrued but unpaid interest on, the Convertible Notes at any time on 30 days' prior notice to the holder.

Conversion Rights	The Convertible Notes, once issued, will be convertible, at the option of the holder, into shares of the Company's Common Stock at the conversion price of $0.95 per share (the "Conversion Price").
Anti-Dilution Protection	In the event the Company issues or is deemed to have issued Common Stock (other than certain excluded issuances) at a purchase price per share that is less than the Conversion Price, the Conversion Price will be re-set to a price equal to 90% of the price at which such shares of Common Stock were or are deemed to have been issued.
Security, Security Interest and Priority	The Company's obligations under the Convertible Notes will be secured by a second priority security interest in and lien on substantially all of the Company's property and real estate, subordinated to the Company's obligations under the WFBC Credit Facility, but senior to the Sutaria Note.

The New Warrants

ITEM	DESCRIPTION
Warrant Shares	When issued in the STAR Note Exchange, the New Warrants will be exercisable for a total aggregate of 1,842,103 shares of Common Stock (each, a "Warrant Share" and together, the "Warrant Shares").
Holders	The New Warrants will be issued to the holders of the STAR Notes, ratably in proportion to their respective percentages of the aggregate principal amount of the STAR Notes.
Exercise Price	$0.95 per share (the "Exercise Price").
Exercise Period	When issued, the New Warrants will be exercisable, in whole or in part, at any time and from time to time during the period beginning on the date of issuance and ending on the fifth anniversary date of such issuance.
Payment for Warrant Shares	Upon each exercise of the New Warrants, payment for the number of Warrant Shares to which that exercise pertains will be in cash, except that if a registration statement covering those Warrant Shares is not effective at the time of exercise, then the exercise may, at the holder's option, be on a cashless basis.
Anti-Dilution Protection	In the event the Company issues or is deemed to have issued Common Stock (other than certain excluded issuances) at a purchase price per share that is less than the Exercise Price, the Exercise Price will be re-set to a price equal to 90% of the price at which such shares of Common Stock were or are deemed to have been issued.

The Amended and Restated Warrants

ITEM	DESCRIPTION
Warrant Shares	Each of the two Amended and Restated Warrants issued in the Warrant Exchange entitles the holder to purchase up to 2,281,914 shares of Common Stock (each, a "Warrant Share" and together, the "Warrant Shares").
Holders	The Amended and Restated Warrants were issued to Tullis and to Aisling in exchange for the B-1 Warrants and the C-1 Warrants, each of which was, except for its exercise price of $1.639 per share, identical in its terms to the Amended and Restated Warrants.
Exercise Price	$0.95 per share (the "Exercise Price").
Exercise Period	The Amended and Restated Warrants are exercisable, in whole or in part, at any time and from time to time during the period beginning on the date of issuance and ending on the fifth anniversary date of such issuance.
Payment for Warrant Shares	Upon each exercise of the Amended and Restated Warrants, payment for the number of Warrant Shares to which that exercise pertains will be in cash, or at the holder's option any such exercise may be on a cashless basis.
Anti-Dilution Protection	In the event the Company issues or is deemed to have issued Common Stock (other than certain excluded issuances) at a purchase price per share that is less than the Exercise Price, the Exercise Price will be re-set to a price equal to 90% of the price at which such shares of Common Stock were or are deemed to have been issued.

The Series D-1 Preferred Stock

ITEM	DESCRIPTION
Title	Series D-1 Convertible Preferred Stock, par value $0.01 per share
Voting Rights	Each share of the Series D-1 Preferred Stock will vote with the Company's Common Stock, and will have that number of votes as is equal to the number of shares of Common Stock into which it is convertible on the record date of the action to be voted upon or consented to, as the case may be.
Liquidation Preference	Upon certain liquidation events set forth in the Certificate of Designations, Preferences and Rights of the Series D-1 Preferred Stock, each share thereof will be entitled to a liquidation payment of $1,000 plus accrued but unpaid dividends.
Dividend Rights	Dividends per share of Series D-1 Preferred Stock will accrue at the rate of 8.25% per annum, payable quarterly in arrears either in cash or, at the Company's option, in shares of restricted Common Stock.
Redemption Provisions	The Company will be required to redeem the Series D-1 Preferred Stock upon the occurrence of certain specified events, including but not limited to

a change in control of the Company, a going private transaction, failure to pay dividends, or a failure to allow conversion.

Number of Shares Authorized	20,825 shares
Number of Shares to be Issued	20,825 shares
Conversion Rights	The Series D-1 Preferred Stock, including any accrued but unpaid dividends thereon, will be convertible by the holder into that number of shares of Common Stock determined by dividing the dollar amount (at the Stated Value of $1,000 per share) to be converted by $0.95 (the “Conversion Price”).
Registration Rights	The holders of the Series D-1 Preferred Stock have demand registration rights pursuant to which the Company must file a registration statement to cover the shares of Common Stock into which the Series D-1 Preferred Stock is convertible within 60 days of the request to do so.
Right to Appoint a Director	For so long as Tullis-Dickerson Capital Focus III, L.P. or any of its affiliates holds at least 25% of the Series D-1 Preferred Stock, it will have the right to appoint one member of the Company’s Board of Directors.
Anti-Dilution Protection	In the event the Company issues or is deemed to have issued Common Stock (other than certain excluded issuances) at a purchase price per share that is less than the Conversion Price, the Conversion Price will be re-set to a price equal to 90% of the price at which such shares of Common Stock were or are deemed to have been issued.

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Our consolidated financial statements for the fiscal years ended June 30, 2007 and 2006, including the notes thereto, together with the report from our independent registered public accounting firm are presented beginning at page F-1.

Our consolidated unaudited financial statements for the three months ended September 30, 2007 and 2006, including the notes thereto, are presented beginning at page F-54.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FISCAL YEARS ENDED JUNE 30, 2007 AND 2006 (in Thousands except per share data)

Results of Operations

Overview

Interpharm Holdings, Inc., (the "Company" or "Interpharm"), through its operating wholly-owned subsidiary, Interpharm, Inc., ("Interpharm, Inc." and collectively with Interpharm, "we" or "us") is engaged in the business of developing, manufacturing and marketing generic prescription strength and over-the-counter pharmaceutical products. As of June 30, 2007, we manufactured and marketed 36 generic pharmaceutical products, which represent various oral dosage strengths for 11 unique products for twenty-five of these products.

As more fully described below, as a result of increased expenses and losses incurred by the Company during the fiscal year ended June 30, 2007, we defaulted on our credit facility with WFBC and, in November 2007, had to raise an additional $8,000 in debt financing. A complete description of the debt financing and a Forbearance Agreement with WFBC may be found below in "Liquidity and Capital Resources."

Net sales for the fiscal year ended June 30, 2007 were $75,587 compared to $63,355 for fiscal year ended June 30, 2006, an increase of $12,232 or 19%. We successfully increased sales of existing products as we continued to expand our distribution with the top tier accounts in retail, wholesale, distributor, and managed care trade classes. However, we had also anticipated launching three new generic pharmaceutical products by June 2007, all of which were delayed. These new products are currently on schedule to be launched in fiscal year ended June 2008.

Our gross margin was 28.7% for the fiscal year ended June 30, 2007, which was somewhat improved over our 27.5% gross margin in the previous year. In the first half of fiscal 2007, we had experienced raw material supply issues, which created backorders, which were fulfilled during the second half of the fiscal year. At the same time, we encountered difficulty in forecasting new customer demand for existing product positions. In an effort to maintain satisfactory customer service levels while solving our raw material supply issues, we created an oversupply and build up of inventory levels. In addition, we lost a large purchaser of our OTC Ibuprofen product at March 31, 2007, due to the customer's FDA regulatory problems, and the customer is no longer purchasing product from us. One result of the foregoing was a significant increase in inventory levels by June 2007.

In parallel, we continued to strengthen our employee infrastructure, particularly in areas such as regulatory affairs and cGMP compliance, and we implemented a new enterprise resource planning IT system needed to accommodate future growth. In addition, we continued spending on our generic pharmaceutical R&D programs at original planned levels. As sales were lower than anticipated, the net result was a significant operating loss for fiscal 2007 which we expect to continue through the first quarter of fiscal 2008. Coupled with the increased inventory levels, the operating losses led to a rapidly worsening cashflow situation towards the end of fiscal 2007. Subsequent to June 2007, we proceeded to identify sources of debt and equity financing which in the completion of $8,000 in subordinated debt financing transactions in November 2007 (see "Liquidity and Capital Resources" for detailed discussion).

With respect to our research and development programs, during fiscal 2007 we filed ten ANDAs and two additional ANDAs owned by the Company but in the name of Tris Pharma. In addition during fiscal 2007, we obtained FDA approval for twelve ANDAs for five unique products which we plan to launch in FY 2008. We are now manufacturing and packaging commercial quantities of some of our current products at our Yaphank facility. The specialized facilities for oral contraceptives, soft gels and high potency products are now operational. We are commencing production of batches for use in conducting bioequivalence studies and the submissions of ANDAs.

We have continued to develop products in areas that are characterized by having high barriers to entry, i.e., related to formulation, technology, patents, analytical and dedicated facilities. We have been aggressive in advancing these high barrier product areas. While the development process has taken longer than planned, we continue to make good progress in these areas.

INTERPHARM HOLDINGS, INC. AND SUBSIDIARIES
(In thousands, except per share data)

Fiscal Year Ended June 30, 2007 compared to Fiscal Year Ended June 30, 2006

	For the Fiscal Year Ended June 30, 2007	For the Fiscal Year Ended June 30, 2006
SALES, Net	$ 75,587	$ 63,355
COST OF SALES	53,920	45,927
GROSS PROFIT	21,667	17,428
Gross Profit Percentage	28.67%	27.51%
OPERATING EXPENSES		
Selling, general and administrative expenses	13,340	11,449
Related party rent expense	103	72
Research and development	18,962	10,674
TOTAL OPERATING EXPENSES	32,405	22,195
OPERATING LOSS	(10,738)	(4,767)
OTHER INCOME (EXPENSES)		
Contract termination expense	(1,655)	
Asset impairment charge	(101)	—
Loss on Sale of Fixed Asset	(99)	(5)
Interest expense, net	(1,275)	(718)
TOTAL OTHER EXPENSES	(3,130)	(723)
LOSS BEFORE INCOME TAXES	(13,868)	(5,490)
INCOME TAX EXPENSE (BENEFIT)	190	(1,700)
NET LOSS	$ (14,058)	$ (3,790)

Net Sales

Net sales for the fiscal year ended June 30, 2007 were $75,587 compared to $63,355 for fiscal year ended June 30, 2006, an increase of $12,232 or 19%. Significant components contributing to our sales growth are set forth in the table below:

	Year ended June			
	2007		2006	
	Sales	% of Sales	Sales	% of Sales
Ibuprofen	$ 31,149	41.2	$ 33,836	53.4
Bactrim(R)	17,471	23.1	4,220	6.7

Naproxen		12,221	16.2		9,401	14.8
Female hormone product		11,199	14.8		8,100	12.8
Hydrocodone/Ibuprofen		2,334	3.1		3,693	5.8
Hydrocodone/Acetaminophen		545	0.7		—	—
All Other Products		668	0.9		4,105	6.5
Total	$	75,587	100%	$	63,355	100%

§ Net sales of Ibuprofen for the year ended June 30, 2007 decreased $2,687, or 7.9%, as compared to sales for the year ended June 30, 2006. The decrease is partially due to supply chain issues incurred during our fiscal year ended June 30, 2007 and partially due to a decrease in demand for a specific strength of Ibuprofen. The decrease in demand is directly related to one of our customer's voluntary suspension of sales of over-the-counter pharmaceuticals as a result of the FDA inspection, which was unrelated to our product. We have been working with our suppliers to obtain adequate supplies of Ibuprofen raw material. We are currently attempting to qualify an additional source of Ibuprofen, and we are making efforts to ensure that our suppliers maintain adequate levels of inventory sufficient to enable us to increase our overall production.

§ For year ended June 30, 2007 we significantly increased our market share of Sulfamethoxazole - Trimethoprim in two strengths 400mg / 80mg commonly referred to as generic Bactrim(R) and 800mg / 160mg or commonly referred to as Bactrim-DS(R) (both, "Bactrim"). Sales increased to $17,471 during the year ended June 2007 from $4,220 for the year ended June 30, 2006, primarily as a result of two significant factors: (i) our entering into sales and marketing arrangements with two major distributors which include net profit sharing arrangements; and (ii) favorable pricing conditions in the market.

§ Naproxen net sales for the year ended June 30, 2007 increased $2,820 or 30%, as compared to sales for the year ended June 2006. The increase is primarily due to our success in increasing our customer base.

§ Net sales of our female hormone products for the year ended June 30, 2007 increased $3,099 or 38.3% compared to sales for the year ended June 2006 due primarily to a higher volume of units shipped during the current fiscal year. As previously reported, as a result of market conditions, on October 27, 2006, we amended our agreement with Pharmaceuticals, Inc. ("Centrix"). Commencing November 2006, Centrix agreed to purchase over a twelve month period, 40% more bottles than the initial year of the agreement at a discounted price with a provision for profit sharing. Under the amended agreement, the parties shared net profits as defined in the agreement. The amendment has a one year term, after which time the original Centrix agreement shall again be in full force and effect.

§ On October 3, 2006, we entered into a termination and release agreement (the "Termination Agreement") with Watson terminating the Manufacturing and Supply Agreement dated as of October 14, 2003 pursuant to which we manufactured and supplied and Watson distributed and sold generic Vicoprofen(R) (7.5 mg hydrocodone bitartrate/200 mg ibuprofen) tablets. As a result of the Termination Agreement we obtained all rights to market this product. Net sales of this product for the year ended June 2007, decreased $1,360 or 36.8% to $2,334 as compared to $3,693 for the year ended June 2006. The decrease is partially due to a decrease in units shipped as well as a decrease in market prices for this product during the year ended June 2007.

§ As a result of our decision to halt the manufacture and sale of Allopurinol and Atenolol under a contract manufacturing agreement, our revenues for these products declined during the fiscal year ended June 30, 2007. Both Allopurinol and Atenolol were manufactured for and shipped to one customer based on quantities ordered by that customer. Revenue from sales of Allopurinol and Atenolol decreased by $2,287 from $2,289 for the year ended June 30, 2006 to $2 for the year ended June 30, 2007. Sales of these product are included in All Other Products in the table above. The manufacturing capacity gained from the decrease in production of these two products is being used for other products. For fiscal 2008 and beyond we anticipate little or no sales of these products.

During the fiscal year ended June 30, 2007, five customers, in the aggregate, accounted for approximately 62% of total sales. For the fiscal year ended June 30, 2006 we had four key customers which accounted for approximately 53%.

Cost of sales / Gross Profits

During year ended June 30, 2007, prices for raw materials remained relatively constant when compared to the prior year. While no assurance can be given, we anticipate this trend to continue, at least for the near future. During the fiscal year ended June 30, 2007, we have incurred increased direct labor and supervisory salaries and related benefits associated with increased production. As part of our expansion plan, we have continued to increase our managerial and production staff. We believe this increase is required and should ultimately support our expansion plan. Additionally, we incurred increased general overhead costs, such as product liability insurance, workers compensation insurance, medical benefits and utilities. We believe these higher costs will likely continue for the near future.

Gross profit for the fiscal year ended June 30, 2007 significantly increased by $4,239, or 24%, to $21,667, compared to $17,428 for the year ended June 30, 2006. In addition, our gross profit percentage remained relatively consistent, increasing 1.2 percentage points from 27.5% for the year ended June 30, 2006 to 28.7% for the year ended June 30, 2007. While direct labor and most overhead expenses have increased to accommodate higher manufacturing throughput in fiscal 2007, the improvement in gross margin is primarily a function of (i) the Company selling higher margin products during the current fiscal year and (ii) greater throughput and relatively higher inventory levels as of June 30, 2007 resulting in higher absorption of labor and overhead and thus, a positive impact on cost of goods sold.

Gross margin percentage can fluctuate as a result of many factors, such as changes in our selling price or the cost of raw materials, as well as increases in cost of labor and general overhead. Fluctuations in our sales volume and product mix affect gross margin dollars. As part of our plan, we are seeking to add new products with higher margins, however, there can be no assurance that sales will increase or cost of sales will not increase disproportionately.

Selling and General and Administrative Expenses

Selling, general and administrative (“SG&A”) expenses include salaries and related costs, commissions, travel, administrative facilities, communications costs and promotional expenses for our direct sales and marketing staff, administrative and executive salaries and related benefits, legal, accounting and other professional fees as well as general corporate overhead.

During the fiscal year ended June 30, 2007, SG&A expenses increased $1,891, or 16.5% to $13,340, as compared to $11,449 during fiscal year end June 2006. When stated as a percentage of net sales, SG&A expenses decreased to 17.6% for the year ended June 2007 as compared to 18.1% for the year ended June 2006.

Significant factors contributing to the dollar increase in SG&A expenses include: an increase of $887 in compensation and related taxes and benefits of sales and administrative staff to support our growth; an increase in professional services of $688, of which $289 relates to costs associated with the implementation of our new ERP system and of which the remainder can be associated with management and IT consulting, an increase in depreciation of $545, primarily due to our second facility becoming operational for general and administrative purposes in July 2006; an increase in rent of $50 and utilities of $196, much of which is associated with our second facility; an increase in computer-related expenses of $202 related to the increase in the number of employees; and an increase in Board Compensation of $194 as a result of a new Board of Directors Compensation Policy. Included in SG&A expense for the fiscal year ended June 2006, was a $621 non-recurring expense related to investment banking services and a non-recurring commission expense of $460 related to a specific contract providing for commissions to one salesman during the first year of sales under a sales agreement with Centrix. The one time expenses incurred during the year ended June 2006 offset the increases noted above in SG&A expenses in the current year.

Research and Development Expenses

Research and development expenses for new products currently in development in our new product pipeline consist primarily of wages, outside development organizations, bioequivalence studies, materials, legal fees, and consulting fees. Research and development expenses increased by $8,288 or 77.6% during the fiscal year ended June 30, 2007 to $18,962 as compared to $10,674 during the fiscal year ended June 2006. This represents an increase in R&D as a percentage of net sales to 25.1% for the fiscal year ended June 30, 2007 as compared to 16.8% for the fiscal year ended June 2006.

The increase was due to: higher compensation expenses of $2,324 primarily related to the expansion of analytical chemist and product formulation staff; an increase of $1,561 for legal services primarily related to patent reviews for products under development or pending launch; an increase in purchases of raw materials of $1,276 necessary for the production of trial batches of new generic pharmaceutical products; $1,128 of increased costs related to bioequivalence studies for new generic pharmaceutical products currently in development; and an increase of $749 for consulting related to new product development.

Our research and development efforts continue to focus in the areas of oral contraceptives, soft gelatin capsules and modified release products, and we are planning to commence bioequivalence studies in each of these areas by December 2007. Work is progressing well in the product area of products coming off patent. As we continue to focus in on these types of pharmaceutical products and as new products are released we anticipate a decline in our research and development costs.

As previously disclosed, during February 2005, we entered into an agreement (“Solids Agreement”), for solid dosage products (“solids”) with Tris. In July 2005, the Solids Agreement was amended. According to the terms of the Solids Agreement, as amended, we will collaborate with Tris on the development, manufacture and marketing of eight solid oral dosage generic products. The amendment to this agreement requires Tris to deliver Technical Packages for two soft-gel products and one additional solid dosage product. Some of the products included in this agreement, as amended, may require us to challenge the patents for the equivalent branded products. This agreement, as amended, provides for payments of an aggregate of $4,800 to Tris, whether or not regulatory approval is obtained for any of the solids products. The Solids Agreement also provides for an equal sharing of net profits for each product, except for one product, that is successfully sold and marketed, after the deduction and reimbursement of all litigation-related and certain other costs. The excluded product provides for a profit split of 60% for us and 40% for Tris. Further, this agreement provides us with a perpetual royalty-free license to use all technology necessary for the solid products in the United States, its territories and possessions.

In April 2006, we further amended the Solids Agreement. This second amendment required Tris to deliver a Technical Package for one additional solid dosage product. Further, terms of this second amendment required the Company to pay to Tris an additional $300 associated with the original agreement.

During October 2006, we entered into a new agreement (“New Liquids Agreement”) with Tris Pharma, Inc. (“Tris”), which terminated the agreement entered into in February 2005, which was for the development and licensing of up to twenty-five liquid generic products (“Liquids Agreement”). According to the terms of the New Liquids Agreement, Tris will, among other things, be required to develop and deliver the properties, specifications and formulations (“Product Details”) for fourteen generic liquid pharmaceutical products (“Liquid Products”). We will then utilize this information to obtain all necessary approvals. Further, under the terms of the New Liquids Agreement Tris will manufacture, package and label each product for a fee. We were required to pay Tris $1,000, whether or not regulatory approval is obtained for any of the liquid products. We have paid in full the $1,000; $250 having been paid during the term of the initial Liquids Agreement; $500 paid upon the execution of the New Liquids Agreement, and the balance of $250 paid December 15, 2006. In addition, Tris is to receive 40% of the net profits, as defined, in accordance with the terms in the New Liquids Agreement.

We further amended the Solids Agreement in October 2006, modifying the manner in which certain costs will be shared as well as clarifying the parties’ respective audit rights.

Interest Expense

Our net interest expense increased approximately $557 to approximately $1,275 for the fiscal year ended June 30, 2007 from $718 for the fiscal year ended June 30, 2006. In an effort to fund our plan, we increased our borrowings from our credit facility with Wells Fargo Business Credit. The additional borrowings were required primarily to fund our research and development efforts, for renovation and construction costs incurred for our second facility and new equipment. In addition to these borrowings being in place for the entire year ended June 30, 2007, we also began to draw down from our line of credit in Q4 2007 and taken additional equipment loans. Our total outstanding debt with Wells Fargo was $26,400 at June 30, 2007 compared to $15,567 at June 30, 2006.

In addition, $87 was included in interest expense for the fiscal year ended June 30, 2007 related to the accreted interest on the Watson Laboratories, Inc. ("Watson") Termination Agreement (the "Termination Agreement") discussed below.

In order to hedge against rising interest rates, we entered into two interest rate swap arrangements. Fair value of the interest rate swaps at June 30, 2007 and 2006 was approximately $10 and $98 and is included in Other Assets. However, it is likely that, as a result of additional borrowings we will incur increases in our interest expense in the future.

Contract Termination Expense

On October 3, 2006, we entered into a Termination and Release Agreement with Watson terminating the Manufacturing and Supply Agreement dated October 14, 2003 (the "Supply Agreement") pursuant to which we manufactured and supplied and Watson distributed and sold generic Vicoprofen(R) (7.5 mg hydrocodone bitartrate/200 mg ibuprofen) tablets, (the "Product"). As a result of entering into the Termination Agreement, we recorded contract termination expense of $1,655 for the year ended June 30, 2007.

Operating Loss

Although our sales and gross margins increased, as a result of our increase in research and development efforts from which we believe we will see the benefits from in the future, along with increases in selling and general and administrative costs, we incurred an operating loss of $10,738 for the year ended June 30, 2007 compared to an operating loss of $4,767 for the year ended June 30, 2006.

Income Taxes

We account for income taxes using the liability method which requires the determination of deferred tax assets and liabilities based on the differences between the financial and tax bases of assets and liabilities using enacted tax rates in effect for the year in which differences are expected to reverse. The net deferred tax asset is adjusted by a valuation allowance, if, based on the weight of available evidence, it is more likely than not that some portion or the entire net deferred tax asset will not be realized. We assess realization of our deferred tax assets based on all available evidence in order to conclude whether it is more likely than not that the deferred tax assets will be realized. Available evidence considered includes, but is not limited to, the our historic operation results, projected future operating earnings results, reversing temporary differences and changing business circumstances. When there is a change in circumstances that causes a change in judgment about the realizability of the deferred tax assets, we may adjust all or a portion of the applicable valuation allowance in the period when such changes occur. For the year ended June 30, 2007 increased our valuation allowance by $4,670 and we recorded income tax expense of $190 as compared to the year ended June 30, 2006, which had a benefit from income tax of $1,700.

Liquidity and Capital Resources

At June 30, 2007 we had an accumulated deficit of $18,831 and operating activities used $14,105 of cash for the year then ended. In order to address our operating loss position and our lack of liquidity, (i) we have completed a series of banking and financing activities in October and November 2007, which are outlined below in "Subsequent Events - Banking and Financing Transactions", and (ii) we are taking various actions to improve profitability and cash flows generated from operations, including:

- Reducing headcount and other operating expenses in different functional areas where possible while still carrying out our future growth plan

- Increasing revenue through the launch of new products, identifying new customers and expanding relationships with existing customers

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Scaling back our research and development activities to levels where we can execute our overall business plan while managing the financial implications

While we believe that the initiatives described above will result in positive cash flows and profitability, there can be no assurance that we will achieve our cash flow and profitability goals, or that we will be able, if necessary, to raise additional capital sufficient to implement our plans. In such event, we may have to revise our plans and significantly reduce our operating expenses, which could have an adverse effect on revenue and operations in the short term.

Subsequent Events - Banking and Financing Transactions

1. On October 26, 2007, the Company and Wells Fargo Business Credit finalized a Forbearance Agreement that terminated on December 31, 2007, which was subsequently amended on November 12, 2007. As of June 30, 2007, the Company had defaulted under the Senior Credit Agreement with respect to (i) financial reporting obligations, including the submission of its annual audited financial statements for the fiscal year ending June 30, 2007, and (ii) financial covenants related to minimum net cash flow, maximum allowable leverage ratio, maximum allowable total capital expenditures and unfinanced capital expenditures for the fiscal year ended June 30, 2007 (collectively, the “Existing Defaults”). WFBC has agreed to waive the Existing Defaults based upon the Borrower’s consummation and receipt of $8,000 related to the issuance of subordinated debt described below. The parties agreed to establish financial covenants for fiscal year 2008 prior to the conclusion of the Forbearance Period, but such agreement was not completed during the Forbearance Period.

2. On November 7, 2007 and November 14, 2007, as required by the Forbearance Agreement, the Company received a total of $8,000 in gross proceeds from the issuance and sale of subordinated debt.

3. On January 10, 2007, the Company and its wholly-owned subsidiary Interpharm, Inc. received notice (the “Notice”) from Wells Fargo that they had defaulted under the Forbearance Agreement with respect to: (i) financial covenants relating to required Income Before Tax for the months ending October 31, 2007 and November 30, 2007, (ii) financial covenants relating to required Net Cash Flow for the months ending October 31, 2007 and November 30, 2007 and (iii) an obligation to have a designated financial advisor provide an opinion as to Holdings and the Company’s ability to meet their fiscal year 2008 projections.

As of January 11, 2008, the Company was obligated to Wells Fargo under the Wells Fargo Agreement in the amount of $31,256,804 (the “Outstanding Amount”). The Notice states that Wells Fargo is not demanding repayment of the Outstanding Amount at this time, but that Wells Fargo reserves the right to do so.
On November 7, 2007, Dr. Maganlal K. Sutaria, the Chairman of the Company’s Board of Directors, and Vimla M. Sutaria, his wife, loaned $3,000 to the Company pursuant to a Junior Subordinated Secured 12% Promissory Note due November 7, 2010 (the “Sutaria Note”). Interest of 12% per annum on the Sutaria Note is payable quarterly in arrears, and for the first 12 months of the note’s term, may be paid in cash, or additional notes (“PIK Notes”), at the option of the Company. Thereafter, the Company is required to pay at least 8% interest in cash, and the balance, at its option, in cash or PIK Notes.

Repayment of the Sutaria Notes is secured by liens on substantially all of the Company’s property and real estate. Pursuant to intercreditor agreements, the Sutaria Notes are subordinated to the liens held by WFBC and the holders of the STAR Notes described below.

On November 14, 2007, the Company issued and sold an aggregate of $5,000 of Secured 12% Promissory Notes due October 1, 2009 (the “STAR Notes”) in the following amounts to the following parties:

Tullis-Dickerson Capital Focus III, L.P. (“TD III”)	$	833
Aisling Capital II, L.P. (“Aisling”)	$	833
Cameron Reid (“Reid”)	$	833
Sutaria Family Realty, LLC (“SFR”)	$	2,500

TD III is an investor in the Company and the holder of its Series B-1 Convertible Preferred Stock. Aisling is also an investor in the Company and the holder of its Series C-1 Convertible Preferred Stock. Reid is the Company's Chief Executive Officer and SFR is owned by Company shareholders who control approximately 54% of the Company's voting stock (the "Major Shareholders"), including Raj Sutaria, who is a Company Executive Vice President.

Interest of 12% per annum on the STAR Notes is payable quarterly in arrears, and may be paid, at the option of the Company, in cash or PIK Notes. Upon the Company obtaining stockholder approval and ratification of the issuance of the STAR Note financing and making the necessary filings with the SEC in connection therewith (the "Stockholder Approval"), which is to occur no earlier than January 18, 2008 and no later than the later of February 28, 2008 or such later date as may be necessary to address SEC comments on the Company's Information Statement on Schedule 14C, the STAR Notes shall be exchanged for:

- Secured Convertible 12% Promissory Notes due 2009 (the "Convertible Notes") in the original principal amount equal to the principal and accrued interest on the STAR Notes through the date of exchange. The conversion price of the Convertible Notes is to be $0.95 per share and interest is to be payable quarterly, in arrears, in either cash or PIK Notes, at the option of the Company;

- Warrants to acquire an aggregate of 1,842 shares of Common Stock (the "Warrants") with an exercise price of $0.95 per share.

Each of the Convertible Notes and Warrants are to have anti-dilution protection with respect to issuances of Common Stock, or common stock equivalents at less than $0.95 per share such that their conversion or exercise price shall be reset to a price equal to 90% of the price at which shares of Common Stock or equivalents are deemed to have been issued.

The repayment of the STAR and Convertible Notes is secured by a second priority lien on substantially all of the Company's property and real estate. Pursuant to intercreditor agreements, the STAR Note financing liens are subordinate to those of WFBC, but ahead, in priority, of the Sutaria Notes.

Also, upon the Company obtaining the Stockholder Approval, the Series B-1 and Series C-1 Convertible Preferred Stock held by TD III and Aisling shall be exchangeable for shares of a new Series D-1 Convertible Preferred Stock, which shall be substantially similar to the B-1 and C-1 Convertible Preferred Stock other than the Conversion price which is to be $0.95 per share instead of $1.5338 per share.

3. Pursuant to the terms of the Securities Purchase Agreements for the Company's Series B-1 and C-1 Convertible Preferred Stock, the consent of TD III and Aisling was required for the issuance of the Sutaria Notes and for the STAR Note financing. In consideration for that consent, the Company has agreed to exchange 2,282 warrants to purchase Company Common Stock held by each of TD III and Aisling with an exercise price of $1.639 per share for new warrants with an exercise price of $0.95 per share. In addition, the Major Shareholders have agreed to give TD III and Aisling tag along rights on certain sales of Company common stock.

Our operations and capital expenditures have been financed through cash flows from operations and the WFBC Credit Facility. For the fiscal year ended June 30, 2007, net cash used in operating activities was $14,105 as compared to cash provided by operating activities of $801 during the fiscal year ended June 30, 2006. Significant factors comprising the net cash used in operating activities for the fiscal year ended June 30, 2007 include: net loss of $14,058, increase in inventory of $9,747, and a decrease in deferred revenue of $3,399, partially offset by a decrease of $1,212 in accounts receivable and an increase in accounts payable, accrued expenses and other liabilities of $5,416. Inventory levels increased significantly due to several factors, as discussed below in "Inventory". The increase in accounts payable, accrued expenses and other payables primarily relates to the increase in purchased inventory items and the overall increase in operating expenses, primarily related to higher research and development costs.

We also recognized several non-cash charges: depreciation and amortization of $2,554, contract termination expense of $1,655 (related to termination of the agreement with Watson Pharmaceuticals), stock-based compensation expense (in accordance with SFAS 123 (R)) amounting to $1,070, a lower of cost or market write down of inventory of $1,157 and deferred tax expense of $195.

During the fiscal year ended June 30, 2007, we used funds in investing activities of $8,296 compared to $8,142 used in investing activities during the fiscal year ended June 30, 2006. These amounts primarily related to capital expenditures of $8,003 in fiscal year ended June 30, 2007 for new machinery, equipment and building renovations as compared to $6,833 of capital expenditures in the prior year. We continue to invest in and develop our Yaphank, NY facility; $4,345 of the total $8,003 in capital expenditures was invested there primarily for purchases of machinery and equipment and building improvements. Most of our research and development activity is conducted there and, as previously reported, we commenced packaging and some manufacturing following an FDA inspection in February 2007. As previously disclosed, we elected not to move forward with the planned construction of a research and development facility in Ahmedabad, India, and on April 25, 2007, we completed the sale of our subsidiary, Interpharm Development Private Limited (“IDPL”) located in Ahmedabad, India to an entity partially owned by two officers of the Company for $161.

During the fiscal year ended June 30, 2007, net cash of $21,035 was provided by financing activities primarily related to (i) the sale of $10,000 of our Series C-1 redeemable convertible preferred stock in September 2006, which generated $9,993 of cash, and (ii) $9,866 in proceeds from drawdown of the WFBC revolving credit facility.

At June 30, 2007, we had $72 in cash and cash equivalents, compared to $1,438 at June 30, 2006.

Bank Financing

On February 9, 2006, we entered into a four-year financing arrangement with Wells Fargo Business Credit ("the WFBC Credit Facility"). This financing agreement provided a maximum credit facility of $41,500 comprised of:

- $22,500 revolving credit facility
- $12,000 real estate term loan
- $ 3,500 machinery and equipment ("M&E") term loan
- $ 3,500 additional / future capital expenditure facility

The funds made available through this facility paid down, in its entirety, the $20,450 owed on the previous credit facility. The WFBC revolving credit facility borrowing base is calculated as (i) 85% of our eligible accounts receivable plus the lesser of 50% of cost or 85% of the net orderly liquidation value of its eligible inventory. The advances pertaining to inventory are capped at the lesser of 100% of the advance from accounts receivable or $9,000. As of June 30, 2007, our remaining availability under the revolving credit facility was $6,708. The $12,000 loan for the real estate in Yaphank, NY is payable in equal monthly installments of $67 plus interest through February 2010 at which time the remaining principal balance is due. As of June 30, 2007, the real estate loan balance outstanding was $10,933. The $3,500 M&E loan is payable in equal monthly installments of $58 plus interest through February 2010 at which time the remaining principal balance is due. During the fiscal year ended June 30, 2007, we borrowed $2,780 under the second capital expenditure facility for the cost of new equipment, and such borrowings are being amortized over 60 months. As of June 30, 2007, the aggregate balance outstanding for both M&E term loans was $5,601, and there was approximately $150 available for additional capital expenditure borrowings.

Under the terms of the WFBC agreement, three stockholders, all related to our Chairman of the Board of Directors, one of whom is an Executive Vice President, were required to provide limited personal guarantees, as well as pledge securities with a minimum aggregate value of $7,500 as security for a portion of the $22,500 credit facility. We were required to raise a minimum of $7,000 through the sale of equity or subordinated debt by June 30, 2006. The shareholder's pledges of marketable securities would be reduced by WFBC either upon our raising capital, net of expenses in excess of $5,000 or achieving certain milestones. As a result of our sale of $10,000 of Series B-1 redeemable convertible preferred stock in May 2006, the limited personal guarantees were reduced by $3,670. Then, in September 2006, our sale of $10,000 Series C-1 redeemable convertible preferred stock eliminated the balance of the personal pledges of marketable securities of $3,830.

The revolving credit facility and term loans bear interest at a rate of the prime rate less 0.5% or, at our option, LIBOR plus 250 basis points. At June 30, 2007, the interest rate on this debt was 7.75%. Pursuant to the requirements of the WFBC agreement, we put in place a lock-box arrangement and we incur a fee of 25 basis points per annum on any unused amounts of this credit facility. The WFBC credit facility is collateralized by substantially all of our assets.

In addition, we are required to comply with certain financial covenants. As of June 30, 2007, we were not in compliance with several covenants, as described above in "Subsequent Events -Banking and Financing Transactions", and we received a waiver of these defaults from WFBC during the Forebearance Period, which ended on December 31, 2007, but received the Notice of default from WFBC on January 10, 2008.

With respect to the real estate term loan and the $3,500 M&E loan, we entered into interest rate swap contracts (the "swaps"), whereby we pay a fixed rate of 7.56% and 8.00% per annum, respectively. The swaps contracts mature in 2010. The swaps are a cash flow hedge (i.e. a hedge against interest rates increasing). As all of the critical terms of the swaps and loans match, they are structured for short-cut accounting under SFAS No. 133, "Accounting For Derivative Instruments and Hedging Activities'" and by definition, there is no hedge ineffectiveness or a need to reassess effectiveness. Fair value of the interest rate swaps at June 30, 2007 was approximately $10 and is included in Other Assets.

As previously disclosed, we entered into agreements with Tris for the development and delivery of over thirty new Technical Packages. The combined costs of these two agreements will approximate $5,800, of which we have paid $5,425 as of June 30, 2007. The balance on the solids agreement, as amended, of $375 could be paid within two years if all milestones are reached. There is no outstanding balance to be paid related to the liquid agreement as of June 30, 2007.

Future cash flows could be aided by utilization of our available Federal net operating loss carryforwards ("NOLs"). At June 30, 2007 we have remaining Federal NOLs of approximately $32,250 available through 2027. As of June 30, 2007, as a result of changes in New York state law, the benefit of the future utilization of State NOLs has been eliminated. Pursuant to Section 382 of the Internal Revenue Code regarding substantial changes in Company ownership, utilization of the Federal NOLs is limited. As a result of losses incurred in fiscal years 2005, 2006 and 2007, which indicate uncertainty as to our ability to generate future taxable income, the “more-likely-than-not” standard has not been met and therefore some amount of the Company’s deferred tax asset may not be realized. As such, a valuation allowance of $5,554 has been established decreasing the total accumulated net deferred tax asset of $11,529 to $5,975.

In addition, at June 30, 2007, we have approximately $986 of New York State investment tax credit carryforwards, expiring in various years through 2022. These carryforwards are available to reduce future New York State income tax liabilities. However, we reserved 100% of the investment tax credit carryforward, which we do not anticipate utilizing.

Watson Termination Agreement

On October 3, 2006, we entered into a termination and release agreement (the “Termination Agreement”) with Watson Laboratories, Inc. (“Watson”) terminating the Manufacturing and Supply Agreement dated October 14, 2003 (the “Supply Agreement”) pursuant to which the we manufactured and supplied and Watson distributed and sold generic Vicoprofen(R) (7.5 mg hydrocodone bitartrate/200 mg ibuprofen) tablets, (the “Product”). Watson was required to return all rights and agreements to us thereby enabling us to market the Product. Further, Watson was required to turn over to us its current customer list for this Product and agreed that, for a period of six months from closing, neither Watson nor any of its affiliates is to solicit sales for this product from its twenty largest customers. In accordance with the Termination Agreement, Watson returned approximately $141 of the Product and then we in turn invoiced Watson $42 for repacking. The net affect was a reduction of $99 to our net sales during the year ended June 30, 2007. In consideration of the termination of Watson’s rights under the Supply Agreement, the we are to pay Watson $2,000 payable at the rate of $500 per year over four years from the first anniversary of the effective date of the termination agreement. Upon entering the Termination Agreement, we determined the net present value of the obligation and accordingly increased Accounts payable, accrued expenses and other liabilities and Contract termination liability by $367 and $1,287, respectively. The imputed interest of $345 will be amortized over the remaining life of the obligation using the effective interest rate method. At June 30, 2007, contract termination liability of $386 and $1,356 are included in Accounts payable, accrued expenses and other liabilities and Contract termination liability, respectively.

Accounts Receivable

Our accounts receivable at June 30, 2007 was $12,945 as compared to $14,212 at June 30, 2006. The average annual turnover ratio of accounts receivable to net sales for the fiscal years ended June 30, 2007 and 2006 was 5.5 and 5.7 turns, respectively. Our turns are calculated on an annual average. Our accounts receivable continue to have minimal risk with respect to bad debts; however this trend cannot be assured.

Inventory

At June 30, 2007, our inventory was $17,295 as compared to $8,706 at June 30, 2006. Our turnover of inventory for the years ended June 30, 2007 and 2006 was 4.15 and 5.20, respectively. Our inventory is current; there are no reserves for obsolescence. Our inventory levels have risen in order to support our growth and overall customer demands.

The Company reduces the carrying value of inventories to a lower of cost or market basis for inventory whose net book value is in excess of market. Aggregate reductions in the carrying value with respect to inventories still on hand at June 30, 2007 that were determined to have a carrying value in excess of market was $1,157. As a result, the Company reduced the net book value of inventory on hand by this amount during the year ended June 30, 2007.

Accounts Payable

Our accounts payable, accrued expenses and other current liabilities increased by approximately $5,892 to $18,542 at June 30, 2007 from $12,650 at June 30, 2006, primarily as a result of a $3,791 increase in accounts payable and accrued expenses related to raw material purchases, which is partially the result of the timing of the receipt of $920 in raw materials at year-end; and an increase in accounts payable and accrued expenses of $935 pertaining to research and development costs, of which $580 of the increase related to legal fees in this area. Additionally, the increase is partially attributable to liabilities incurred in relation to fixed asset additions, specifically, the Company has approximately $516 included in accounts payable and accrued expenses at June 30, 2007 related to the acquisition of our new ERP system.

Cash

During the year ended June 30, 2007, cash decreased $1,366 from $1,438 at June 30, 2006 to $72 at June 30, 2007. For the year ended June 30, 2007 we funded our business from bank debt, operations and sale of Series C-1 redeemable convertible preferred stock.

Our Obligations

As of June 30, 2007, our obligations and the periods in which they are scheduled to become due are set forth in the following table:

Obligation	Total	Due in less than 1 Year	Due in 1-3 Years	Due in 3-5 Years	Due after 5 Years
Real Estate and M&E Term Loans (a)	$ 16,534	$ 2,170	$ 14,364	$ —	$ —
Capital lease	145	21	77	47	—
Line of Credit	9,866	9,866	—	—	—
Operating lease and software license	10,547	1,188	2,026	1,902	5,431
Other long-term liabilities reflected on the Registrants Balance Sheet under GAAP	2,000	500	1,000	500	—
Total cash obligations	$ 39,092	$ 13,745	$ 17,467	$ 2,449	$ 5,431

In addition to the information presented in the table above, there is a balance on the Tris solids agreement, as amended, of $375 which could be paid by us if certain milestones are reached.

(a) The Real Estate Term Loan of $12,000 is for the real estate in Brookhaven, NY, is payable in equal monthly installments of $67 plus interest through February 2010 at which time the remaining principal balance is due. The M&E Term Loans are payable in equal monthly installments of $114 plus interest through February 2010 at which time the remaining principal balance is due. With respect to additional capital expenditures, we are permitted to borrow 90% of the cost of new equipment purchased to a maximum of $3,500 in borrowings amortized over 60 months. As of June 30, 2007, there is approximately $150 available for additional capital expenditure borrowings.

Leases

We lease an entire building in Hauppauge, New York, pursuant to a non-cancellable lease expiring in October, 2019, which houses our manufacturing, warehousing and some executive offices. The leased building is approximately 100 square feet and is located in an industrial/office park. The current annual lease payments to the landlord, Sutaria Family Realty, LLC, are $660. Sutaria Family Realty, LLC is owned by Mona Rametra, Perry Sutaria and Raj Sutaria. Upon a change in ownership of the Company, and every three years thereafter, the annual base rent will be adjusted to fair market value, as determined by an independent appraisal. There are no tenants in the building other than us.In January 2007 the Company entered into a seven year lease for approximately 20 square feet of office space. The lease provides us an option to extend the lease for a period of three years. According to the terms of the lease the base annual rental for the first year will be $261 and will increase by 3% annually thereafter. Further, the Company is required to pay for renovations to the facility, currently estimated at approximately $300.

INTERPHARM HOLDINGS, INC. AND SUBSIDIARIES
(In thousands, except per share data)

Fiscal Year Ended June 30, 2006 compared to Fiscal Year Ended June 30, 2005

	For the Fiscal Year Ended June 30, 2006	For the Fiscal Year Ended June 30, 2005
SALES, Net	$ 63,355	$ 39,911
COST OF SALES	45,927	30,839
GROSS PROFIT	17,428	9,072
Gross Profit Percentage	27.51%	22.73%
OPERATING EXPENSES		
Selling, general and administrative expenses	11,449	5,092
Related party rent expense	72	72
Research and development	10,674	4,003
TOTAL OPERATING EXPENSES	22,195	9,167
OPERATING LOSS	(4,767)	(95)
OTHER INCOME (EXPENSES)		
Gain on sale of marketable securities	—	9
Loss on sale of fixed asset	(5)	—
Interest expense, net	(718)	(136)
TOTAL OTHER EXPENSES	(723)	(127)
LOSS BEFORE INCOME TAXES	(5,490)	(222)
BENEFIT FROM INCOME TAXES	(1,700)	(73)
NET LOSS	$ (3,790)	$ (149)

Net Sales

Net sales for the fiscal year ended June 30, 2006 were $63,355 compared to $39,911 for fiscal year ended June 30, 2005, an increase of $23,444 or 58.7%. Significant components contributing to our growth of existing products were those set forth in the table below:

Product	Year over year increase in net sales	
Ibuprofen	$	5,866
Naproxen		7,721
Hydrocodone / Ibuprofen		1,166
Total	$	14,753

§ The increase in net sales of Ibuprofen was primarily the result of an expanded customer base and improvements in manufacturing and packaging which enabled us to increase output and modest cost of materials reductions.

§ An expanded customer base, as well as obtaining a U.S. Government contract to supply Naproxen to various governmental agencies valued at approximately $3,900 for the twelve month period beginning September 2005 were key factors contributing to the $7,721 increase in sales of Naproxen. The contract includes four one-year option periods.

§ On a fiscal year over year basis, we had an increase of more than $1,166 from sales of Hydrocodone 7.5 mg/Ibuprofen 200 mg, our generic version of Vicoprofen(R), which was launched during the three month period ended December 31, 2004, and Reprexain(R) (Hydrocodone 5.0 mg/Ibuprofen 200 mg). The results for the periods reported include additional revenue derived from a profit sharing arrangement for these products.

During the fiscal year ended June 30, 2006, we began to see the positive effects of our expansion plan which commenced in 2005. Two new products were launched which contributed greatly to our revenue growth. As we continue our planned product line expansion we anticipate that fiscal year 2007 should witness the launching of new products as well; however there can be no assurance we will be successful in achieving our plan. The two new products for fiscal 2006 were:

§ As reported in our Current Report on Form 8-K filed with the SEC on July 18, 2005, we entered into an agreement with Centrix Pharmaceutical, Inc. ("Centrix") for the sale of a female hormone product, which is distributed in two strengths. This product generates a higher gross margin compared to our other products. The agreement commenced upon the first shipment of the product to Centrix in August, 2005. Centrix was required to purchase a minimum $11,500 of the product during the first twelve month period with the option to purchase an additional $2,000 of product. For the twelve month period ended June 30, 2006, we shipped approximately $8,100 of the female hormone product to Centrix. We will ship approximately $5,400 of product by September 30, 2006. We have renegotiated the agreement with Centrix for the up coming year and we anticipated sales during fiscal 2007 of the product to exceed fiscal year 2006 totals. In the event that the agreement is terminated at any time, or for any reason, we maintain the right to market the product alone or with a third party.

- In September, 2005, we launched Sulfamethoxazole and Trimethoprim ("SMT") single and double strength tablets, which are sold by the innovator under the brand-name Bactrim(R). SMT is a widely used antibiotic used to treat infections such as urinary tract infections, bronchitis, ear infections (otitis), traveler's diarrhea, and Pneumocystis carinii pneumonia. Sales during fiscal 2006 of these products approximated $4,200.

As a result of our decision to greatly reduce and ultimately halt the manufacture and sale of Allopurinol and Atenolol under a contract manufacturing agreement, our revenues for these products declined during the fiscal year ended June 30, 2006. Both Allopurinol and Atenolol were manufactured for and shipped to one customer based on quantities ordered by that customer. Revenue from sales of Allopurinol and Atenolol decreased by approximately $4,700 from $7,100 for the year ended June 30, 2005 to $2,400 for the year ended June 30, 2006. The manufacturing capacity gained from the decrease in production of these two products is being used for other products.

The fluctuations in revenue by product were generally not attributable to any changes in our pricing which, for our entire product line, remained relatively stable.

During the fiscal year ended June 30, 2006, four key customers, in the aggregate, accounted for approximately 53% of total sales. For the fiscal year ended June 30, 2005 we had three key customers which accounted for approximately 56%

Cost of sales / Gross Profits

During the year ended June 30, 2006, prices for our raw materials remained relatively constant. While no assurance could be given, we anticipated this trend to continue, at least for the near future. During the fiscal year ended June 30, 2006, prices for packaging components increased. It is uncertain as to whether or not these costs will continue to rise. We have incurred increased direct labor and supervisory salaries and related benefits associated with increased production. As part of our expansion plan, we have increased managerial and production staff. We believed this increase is required and should ultimately support our expansion plan. Additionally, incurred increased general overhead costs, such as product liability insurance, workers compensation insurance, medical benefits and utilities.

Gross profit for the fiscal year ended June 30, 2006 significantly increased $8,356, or 92%, to $17,428, compared to $9,072 for the year ended June 30, 2005. In addition, our gross profit percentage increased 4.8 percentage points from 22.7% for the year ended June 30, 2005 to 27.5% for the year ended June 30, 2006. This increase is primarily due to sales of our new products: Bactrim(R) and our female hormone therapy products which both generate higher gross margins compared to our remaining products. Gross margins for the remaining products were generally consistent with the prior year.

Gross margin percentage can fluctuate as a result of many factors, such as changes in our selling price or the cost of raw materials, as well as increases in cost of labor and general overhead. Fluctuations in our sales volume and product mix affect gross margin dollars. As part of our plan, we are seeking to add new products with higher margins, however, there can be no assurance that sales will increase or cost of sales will not increase disproportionately.

Selling and General and Administrative Expenses

Selling, general and administrative expenses include salaries and related costs, commissions, travel, administrative facilities, communications costs and promotional expenses for our direct sales and marketing staff, administrative and executive salaries and related benefits, legal, accounting and other professional fees as well as general corporate overhead.

During the fiscal year ended June 30, 2006, selling, general and administrative expenses increased approximately $6,357 to approximately $11,449, or 18.1% of net sales from approximately $5,092 or 12.8% of net sales, during fiscal year end June 30, 2005.

Significant factors contributing to this increase include: necessary increases in the staffing of administrative and sales areas to support our growth of $1,954; related payroll taxes and benefits of $496; increased commission expenses and freight expenses of $314 and $234, respectively, both of which are attributable to our higher sales; $600 for investment banking services; increased accounting and legal costs of $284, primarily related to the refinancing of our bank debt and sale of our Series B-1 preferred stock; an increase in general insurance of $229; increased rent, utilities and taxes of $200; an increase in depreciation of non-manufacturing assets of $105; and the recognition of a non cash charge of $1,195` as a result of our adoption of the fair value recognition provisions of Statement of Financial Accounting Standards (“SFAS”) No. 123 (Revised 2004), “Share-Based Payment,” (“SFAS 123(R)”). Included in the $1,195 was a non-cash charge related to the modification of an option grant as a result the death of an executive officer. Adoption of SFAS 123(R) requires us to report a non-cash expense for the ratable portion of the fair value of employee stock option awards of unvested stock options over the remaining vesting period. Previously we elected to follow the intrinsic value method in accounting for our stock-based employee compensation arrangements as defined by Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," and related interpretations including Financial Accounting Standards Board Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation".

Research and Development Expenses

Research and development expenses for new products currently in development in our new product pipeline consist primarily of wages, outside development organizations, bioequivalence studies, materials, legal fees, and consulting fees. During the fiscal year ended June 30, 2006 we incurred $10,674 in research and development expenses, which is $6,671 greater than the prior year amount of $4,003. We believe that research and development expenses, as a percentage of our net sales, will be substantially higher in the future as we seek to expand our product lines. While we believed increased spending for research and development efforts will allow us to add obtain approvals for new products, there can be no assurance we will be successful in the commercialization.

A significant component of our expansion plan includes two agreements with Tris Pharma, Inc. (“Tris”). One of the agreements is for the development and licensing of twenty-five liquid generic products (“Liquids Agreement”). In the event that Tris delivers twenty-five successful technical packages, of which there can be no assurance, we will be required to pay Tris $3,000.

In accordance with the terms of this agreement, we make payments as various milestones are achieved. In addition, Tris is to receive a royalty of between 10% and 12% of net profits resulting from the sales of each product. We are entitled to offset the royalty payable to Tris each year, at an agreed upon rate, to recoup the development fees paid to Tris under the Liquids Agreement.

The second agreement, as amended, pertains to the solid dosage products (“solids”), pursuant to which we are to collaborate with Tris on the development, manufacture and marketing of eight solid oral dosage generic products. The amendment to this agreement requires Tris to deliver technical packages for two softgel products. Further, the terms of this amendment require us pay to Tris $750 based upon various Tris milestone achievements. Some products included in this agreement, as amended, may require us to challenge the patents for the equivalent branded products. This agreement, as amended, provides for payments of an aggregate of $4,500 to Tris, whether or not regulatory approval is obtained for any of the solids products. The agreement for solids also provides for an equal sharing of net profits for each product, except for one product, if it is successfully sold and marketed, after the deduction and reimbursement of all litigation-related and certain other costs. The excluded product provides for a profit split of 60% for the Company and 40% for Tris. Further, this agreement provides us with a perpetual royalty-free license to use all technology necessary for the solid products in the United States, its territories and possessions.

In April, 2006, the solids agreement was further amended. This second amendment requires Tris to deliver a Technical Package for one additional solid dosage product. Further, terms of this second amendment will requires us to pay to Tris an additional $300 after it has paid the initial aggregate amounts associated to the original agreement.

For the fiscal year ended June 30, 2006, we recorded as a research and development expense approximately $2,110 in connection with these agreements. Further, since inception, we have incurred approximately $3,510 of research and development costs associated with the Tris agreements. The combined costs of these agreements could aggregate up to $7,800. The balance on the liquid agreement of $2,750 could be paid within three years if all milestones are reached. The balance on the solids agreement, as amended, of $1,675 could be paid within two years if all milestones are reached.

During the fiscal year ended June 30, 2006, we filed seventeen ANDAs.

Interest Expense

Our interest expense, net increased approximately $583 to approximately $718 for the fiscal year ended June 30, 2006 from $136 for the fiscal year ended June 30, 2005. In an effort to fund our plan, in February, 2006, we increased our borrowing capabilities through a new credit facility entered into with Wells Fargo Business Credit. The additional borrowings were required primarily to fund our research and development efforts, for renovation and construction costs incurred for our second facility and new equipment. In order to hedge against rising interest rates, we entered into two interest rate swap arrangements. As of June 30, 2006, we have saved approximately $98 as a result of these swaps agreements.

Operating Loss

Although our sales and gross margins increased, as a result of our increase in research and development efforts from which we believe we will see the benefits from in the future, along with increases in selling and general and administrative costs, we incurred an operating loss of $5,490 for the year ended June 30, 2006 compared to an operating loss of $222 for the year ended June 30, 2005.

Income Taxes

For the year ended June 30, 2006 we recorded an income tax benefit of $1,700, an increase in the benefit of $1,627 compared to the year ended June 30, 2005 which had a benefit from income tax of $73.

We account for income taxes using the liability method which requires the determination of deferred tax assets and liabilities based on the differences between the financial and tax bases of assets and liabilities using enacted tax rates in effect for the year in which differences are expected to reverse. The net deferred tax asset is adjusted by a valuation allowance, if, based on the weight of available evidence, it is more likely than not that some portion or all of the net deferred tax asset will not be realized. Our net deferred tax asset at June 30, 2006 was $6,170 and $4,413 at June 30, 2005.

Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations discusses our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires that we make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, we evaluate judgments and estimates made, including those related to revenue recognition, inventories, income taxes and contingencies including litigation. We base our judgments and estimates on historical experience and on various other factors that it believes to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We consider the following accounting policies to be most critical in understanding the more complex judgments that are involved in preparing its financial statements and the uncertainties that could impact results of operations, financial condition and cash flows.

Revenue Recognition

We recognize product sales revenue when title and risk of loss have transferred to the customer, when estimated provisions for chargebacks and other sales allowances including discounts, rebates, etc., are reasonably determinable, and when collectibility is reasonably assured. Accruals for these provisions are presented in the consolidated financial statements as reductions to revenues.

We purchased raw materials from one supplier for the year ended June 30, 2007 and two suppliers for the years ended June 30, 2006 and 2005, which are manufactured into finished goods and sold back to this supplier as well as to other customers. We can, and do, purchase raw materials from other suppliers. Pursuant to Emerging Issues Task Force, (“EITF”) No. 99-19, “Reporting Revenue Gross as a Principal Versus Net as an Agent,” the Company recorded sales to, and purchases from, this supplier on a gross basis. Sales and purchases were recorded on a gross basis since we (i) have a risk of loss associated with the raw materials purchased, (ii) convert the raw material into a finished product based upon developed specifications, (iii) have other sources of supply of the raw material, and (iv) have credit risk related to the sale of such product to the suppliers. For the year ended June 30, 2007, we purchased raw materials from this supplier totaling approximately $10,714, and sold finished goods to this supplier totaling approximately $1,054. For the years ended June 30, 2006 and 2005, we purchased raw materials from two suppliers, which were manufactured into finished goods and sold back to these suppliers totaling approximately $10,608 and $9,251, respectively, and sold finished goods to such suppliers totaling approximately $6,110, and $17,414, respectively. These purchase and sales transactions are recorded at fair value in accordance with EITF Issue No. 04-13, “Accounting for Purchases and Sales of Inventory with the Same Counterparty”.

In addition, we are party to supply agreements with certain pharmaceutical companies under which, in addition to the selling price of the product, we receive payments based on sales or profits associated with these products realized by its customer. We recognize revenue related to the initial selling price upon shipment of the products as the selling price is fixed and determinable and no right of return exists. The additional revenue component of these agreement's are recognized by us at the time our customers record their sales and is based on pre-defined formulas contained in the agreements. Receivables related to this revenue of $594 and $620 and at June 30, 2007 and 2006, respectively, are included in "Accounts receivable, net" in the accompanying Consolidated Balance Sheets.

Sales Returns and Allowances

At the time of sale, we simultaneously record estimates for various costs, which reduce product sales. These costs include estimates of chargebacks and other sales allowances. In addition, we record an allowance for rebates, including Medicaid rebates and shelf-stock adjustments when the conditions are appropriate. Estimates for sales allowances such as chargebacks are based on a variety of factors including actual return experience of that product or similar products, rebate arrangements for each product, and estimated sales by our wholesale customers to other third parties who have contracts with us. Actual experience associated with any of these items may be different than our estimates. We regularly review the factors that influence our estimates and, if necessary, make adjustments when we believe that actual product returns, credits and other allowances may differ from established reserves.

Sales Incentives

In accordance with the terms and conditions of an agreement entered into during the fiscal year ended June 30, 2006, we have offered a sales incentive to one of our customers in the form of an incentive volume price adjustment. We account for sales incentives in accordance with EITF 01-9, "Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of Vendor's Products)" ("EITF 01-9"). The terms of this volume based sales incentive required the customer to purchase a minimum quantity of our products during a specified period of time. The incentive offered was based upon a fixed dollar amount per unit sold to the customer. We made an estimate of the ultimate amount of the incentive the customer would earn based upon past history with the customer and other facts and circumstances. We had the ability to estimate this volume incentive price adjustment, as there did not exist a relatively long period of time for the particular adjustment to be earned. Any change in the estimated amount of the volume incentive was recognized immediately using a cumulative catch-up adjustment. In accordance with EITF 01-9, we recorded the provision for this sales incentive when the related revenue is recognized. Our sales incentive liability may prove to be inaccurate, in which case we may have understated or overstated the provision required for these arrangements. Therefore, although we make our best estimate of our sales incentive liability, many factors, including significant unanticipated changes in the purchasing volume of our customer, could have significant impact on the our liability for sales incentives and our reported operating results. The specific terms of this agreement which related to sales incentives expired in October 2006. For the year ended June 30, 2007, we recognized sales incentive revenue of $3,399 related to this agreement.

Inventory

Inventories are valued at the lower of cost (first-in, first-out basis) or market value. Losses from the write-down of damaged, nonusable, or otherwise nonsalable inventories are recorded in the period in which they occur.

Income Taxes

We account for income taxes using the liability method which requires the determination of deferred tax assets and liabilities based on the differences between the financial and tax bases of assets and liabilities using enacted tax rates in effect for the year in which differences are expected to reverse. The net deferred tax asset is adjusted by a valuation allowance, if, based on the weight of available evidence, it is more likely than not that some portion or all of the net deferred tax asset will not be realized. Our net deferred tax asset at June 30, 2007 was $5,975 and $6,170 at June 30, 2006.

Research and Development

Pursuant to SFAS No. 2 “Accounting for Research and Development Costs,” research and development costs are expensed as incurred or at the date payment of non-refundable amounts become due, whichever occurs first. Research and development costs, which consist of salaries and related costs of research and development personnel, fees paid to consultants and outside service providers, raw materials used specifically in the development of its new products and bioequivalence studies. Pre-approved milestone payments due under contract research and development arrangements are expensed when the milestone is achieved.

Stock Based Compensation

Effective July 1, 2005, we adopted the fair value recognition provisions of SFAS No. 123 (Revised 2004), “Share-Based Payment,” (“SFAS No. 123(R)”), using the modified-prospective-transition method. As a result, our net income before taxes for the years ended June 30, 2007 and 2006 are $1,070 and $1,195 lower than if it had continued to account for share-based compensation under Accounting Principles Board (“APB”) opinion No. 25, “Accounting for Stock Issued to Employees” (“APB No. 25”).

Accounts Receivable / Chargebacks

Accounts receivable are comprised of amounts owed to us through the sales of our products throughout the United States. These accounts receivable are presented net of allowances for doubtful accounts, sales returns, discounts, rebates and customer chargebacks. Allowances for doubtful accounts were approximately $30 and $101 at June 30, 2007 and 2006, respectively. The allowance for doubtful accounts is based on a review of specifically identified accounts, in addition to an overall aging analysis. Judgments are made with respect to the collectibility of accounts receivable based on historical experience and current economic trends. Actual losses could differ from those estimates. Allowances relating to discounts, rebates, and customer chargebacks were $4,865 and $2,315 at June 30, 2007 and June 30, 2006, respectively. We sell some of our products indirectly to various government agencies referred to below as “indirect customers.” We enter into agreements with our indirect customers to establish pricing for certain products. The indirect customers then independently select a wholesaler from which to actually purchase the products at these agreed-upon prices. We will provide credit to the selected wholesaler for the difference between the agreed-upon price with the indirect customer and the wholesaler’s invoice price if the price sold to the indirect customer is lower than the direct price to the wholesaler. This credit is called a chargeback. The provision for chargebacks is based on expected sell-through levels by our wholesale customers to the indirect customers, and estimated wholesaler inventory levels. As sales to the large wholesale customers increase, the reserve for chargebacks will also generally increase. However, the size of the increase depends on the product mix. We continually monitor the reserve for chargebacks and make adjustments to the reserve as deemed necessary. Actual chargebacks may differ from estimated reserves.

Recently Issued Accounting Pronouncements

In November 2006, The Emerging Issues Task Force (“EITF”) reached a final consensus in EITF Issue 06-6 “Debtor’s Accounting for a Modification (or Exchange) of Convertible Debt Instruments” (“EITF 06-6”). EITF 06-6 addresses the modification of a convertible debt instrument that changes the fair value of an embedded conversion option and the subsequent recognition of interest expense for the associated debt instrument when the modification does not result in a debt extinguishment pursuant to EITF 96-19, “Debtor’s Accounting for a Modification or Exchange of Debt Instruments,”. The consensus should be applied to modifications or exchanges of debt instruments occurring in interim or annual periods beginning after November 29, 2006. The adoption of EITF 06-6 did not have a material effect on our consolidated financial position, results of operations or cash flows.

In November 2006, The Financial Accounting Standards Board (“FASB”) ratified EITF Issue No. 06-7, “Issuer’s Accounting for a Previously Bifurcated Conversion Option in a Convertible Debt Instrument When the Conversion Option No Longer Meets the Bifurcation Criteria in FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities” (“EITF 06-7”). At the time of issuance, an embedded conversion option in a convertible debt instrument may be required to be bifurcated from the debt instrument and accounted for separately by the issuer as a derivative under of Financial Accounting Standards (“FAS”) 133, based on the application of EITF 00-19. Subsequent to the issuance of the convertible debt, facts may change and cause the embedded conversion option to no longer meet the conditions for separate accounting as a derivative instrument, such as when the bifurcated instrument meets the conditions of Issue 00-19 to be classified in stockholders’ equity. Under EITF 06-7, when an embedded conversion option previously accounted for as a derivative under FAS 133 no longer meets the bifurcation criteria under that standard, an issuer shall disclose a description of the principal changes causing the embedded conversion option to no longer require bifurcation under FAS 133 and the amount of the liability for the conversion option reclassified to stockholders' equity. EITF 06-7 should be applied to all previously bifurcated conversion options in convertible debt instruments that no longer meet the bifurcation criteria in FAS 133 in interim or annual periods beginning after December 15, 2006, regardless of whether the debt instrument was entered into prior or subsequent to the effective date of EITF 06-7. Earlier application of EITF 06-7 is permitted in periods for which financial statements have not yet been issued. The adoption of EITF 06-7 did not have a material effect on our consolidated financial position, results of operations or cash flows.

In February 2006, the FASB issued SFAS No. 155 "Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140" ("SFAS 155"). SFAS 155 clarifies certain issues relating to embedded derivatives and beneficial interests in securitized financial assets. The provisions of SFAS 155 are effective for all financial instruments acquired or issued after fiscal years beginning after September 15, 2006. We are currently assessing the impact that the adoption of SFAS 155 will have on its financial position and results of operations.

In June 2006, the FASB issued Interpretation No. 48, “Accounting for Uncertainty in Income Taxes”, (“FIN 48”). This interpretation clarified the accounting for uncertainty in income taxes recognized in accordance with SFAS No. 109, “Accounting for Income Taxes” (“SFAS No.109”). Specifically, FIN 48 clarifies the application of SFAS No. 109 by defining a criterion that an individual tax position must meet for any part of the benefit of that position to be recognized in an enterprise’s financial statements. Additionally, FIN 48 provides guidance on measurement, derecognition, classification, interest and penalties, accounting in interim periods of income taxes, as well as the required disclosure and transition. This interpretation is effective for fiscal years beginning after December 15, 2006. We are currently assessing the impact that the adoption of FIN 48 will have on its financial position and results of operations.

In March 2006, the FASB issued SFAS No. 156, “Accounting for Servicing of Financial Assets” (“SFAS 156”), which amends SFAS 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities”, with respect to the accounting for separately recognized servicing assets and servicing liabilities. SFAS 156 permits the choice of the amortization method or the fair value measurement method, with changes in fair value recorded in income, for the subsequent measurement for each class of separately recognized servicing assets and servicing liabilities. The statement is effective for years beginning after September 15, 2006, with earlier adoption p