

PAION Q1#2010

Consolidated Financial Interim Report for the First Quarter 2010

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PAION AG

Key Figures

(all figures in KEUR unless otherwise noted)	Q1 2010	Q1 2009
Revenues	742	405
Research and development expenses	-2,483	-2,616
General and administrative expenses	-1,103	-1,152
Net loss for the period	-2,871	-3,327
Earnings per share (in EUR), basic	-0.12	-0.14
Earnings per share (in EUR), diluted	-0.12	-0.14

	Q1 2010	Q1 2009
Cash flows from operating activities	-3,480	-3,573
Cash flows from investing activities	-12	-25
Cash flows from financing activities	-146	-164
Average number of group employees	29	30

	31 March 2010	31 Dec. 2009
Intangible assets	11,147	11,380
Cash and cash equivalents	19,238	22,871
Equity	16,503	19,304
Non-current liabilities	11,637	12,033
Balance sheet total	32,135	35,550
Equity ratio	51.4%	54.3%

Interim Group Management Report for the Three-Month Period Ending 31 March 2010

Overview

- PAION finalises preparation for Phase IIb study with CNS 7056
- PAION's partners achieve development milestones that trigger milestone payments
- PAION improves its financial position strongly with an equity facility and milestone payments extending its cash reach significantly

In the first quarter of 2010 PAION concentrated on the development of CNS 7056. Based on the results of the Phase Ib and Phase IIa studies PAION completed the preparations to conduct a Phase IIb study with patients undergoing a colonoscopy. The aim of this study is to refine the optimal dose regimen for Phase III with a multi-centre trial. The patient enrolment will start shortly as the regulatory process is now completed.

In early February 2010, PAION announced that its development partner Ono Pharmaceutical had initiated the first Japanese Phase I study with CNS 7056. Ono is developing CNS 7056 for the Japanese market initially for the induction and maintenance of anaesthesia which requires continuous infusion. The first subject in the Japanese Phase I study was enrolled in April 2010 after the balance sheet date. This triggered the first milestone payment of USD 1 million from Ono; payment is expected in May 2010.

At the end of February 2010, PAION reported that its license partner H. Lundbeck A/S had presented data from a post-hoc analysis using Desmoteplase in acute ischaemic stroke at the International Stroke Conference in San Antonio, Texas. The findings from the post-hoc analysis of the DIAS-2 trial performed by PAION provided the basis for the design of the currently ongoing clinical Phase III programme (DIAS-3 and DIAS-4 studies) which aims to enrol 800 patients with acute ischaemic stroke. Lundbeck expects study completion in 2011.

In mid March 2010, PAION reported that Lundbeck had initiated a clinical Phase II trial with Desmoteplase in the treatment of acute ischaemic stroke (DIAS-1) in Japan. This study is required for the approval of the substance for the Japanese market. Lundbeck expects to take approximately 1.5 years to conduct the study.

In March 2010, our licensee Acorda Therapeutics filed an IND (Investigational New Drug) application for the substance GGF2. This triggered the obligation to pay the first milestone of USD 0.5 million; the payment was received in April 2010. On 20 April 2010 Acorda announced the IND acceptance which triggered the obligation to pay the second milestone of USD 0.5 million; the payment is expected in May 2010. Acorda plans to begin a clinical Phase I study with GGF2 in heart failure patients by mid 2010.

In May 2010 PAION entered into an equity facility agreement for EUR 15 million with Commerce Court Small Cap Value Fund Ltd. (CCSCVF) managed by Acqua Capital Management Inc., Toronto, Canada. This equity facility gives PAION the right to issue new shares out of the existing authorised capital in multiple tranches to CCSCVF against a cash

contribution. PAION intends to use this facility in the first instance to strengthen its cash position and extend its cash reach. The equity facility is described in more detail on page 12 under “Equity Facility”.

The loss for the first three months of 2010 of KEUR -2,871 was KEUR 456 lower than in the corresponding prior-year period (KEUR -3,327). Compared to the prior-year period revenues increased mainly due to the milestone from Acorda in the amount of USD 0.5 million for the development of GGF2. Research and development expenses and administrative expenses decreased slightly compared to the prior-year period. Cash and cash equivalents decreased by KEUR 3,634 in the first quarter 2010 and amounted to KEUR 19,238 compared to KEUR 22,871 as of 31 December 2009.

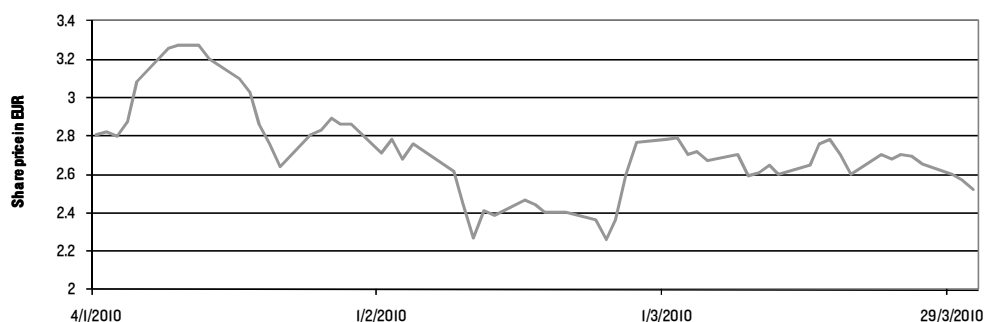
PAION's cash and cash equivalents of EUR 19 million as of 31 March 2010, the milestone payments due from Acorda and Ono in the second quarter 2010 and the expected cash inflows from a partial use of the equity facility secure, based on the current cost structure including the Phase IIb trial with CNS 7056, a cash reach until the middle of 2012.

Share Performance

Based on the positive development of our research projects, the closing price of the PAION share on Xetra reached EUR 3.27 on 12 January 2010, marking a new peak price since October 2007. Thereafter, driven by profit-taking, the share price decreased steadily. The lowest point on Xetra for the first quarter 2010 was reached on 23 February 2010 at EUR 2.26. The share price recovered continuously towards the end of the quarter, closing again at EUR 2.52, thereby being almost identical to the closing price on 31 December 2009 of EUR 2.55.

The overall average daily trading volume (Xetra, Frankfurt Stock Exchange resp. all German Stock Exchanges) amounted to 94,002 shares during the first three months of 2010. During the whole of 2009 the average daily trading volume was 61,410 shares. In the first three months of 2010 5.8 million shares (24% of total shares) were traded.

Development of the PAION Share Price (Xetra) in the First Three-Month Period 2010



Overview of Research and Development Activities

CNS 7056/Remimazolam (pINN)

CNS 7056 is an innovative short-acting general anaesthetic/sedative that is being developed by PAION initially for use in minor medical interventions (procedural sedation). Sedatives are used, for example, in endoscopic procedures such as colonoscopies. After intravenous administration to human volunteers as well as patients CNS 7056 rapidly induces the desired sedation. Importantly, for the benefit of the patient, this sedative effect quickly disappears again. This implies that the patient can be selectively sedated for the duration of the intervention and rapidly regains full consciousness after the procedure. This rapid offset of the effect of the substance is due to its metabolism by tissue esterase enzymes that are widely distributed throughout the body. CNS 7056 is being developed as a sedative agent for day case procedures and for the induction and maintenance of anaesthesia. It could also be used as a sedative during artificial respiration in the Intensive Care Unit (ICU). Our development partner Ono is developing CNS 7056 for the Japanese market initially for the induction and maintenance of anaesthesia.

The proposed international nonproprietary name (pINN) for CNS 7056 by the World Health Organisation since February 2010 is Remimazolam.

Clinical Development

The clinical studies performed with CNS 7056 comprise two Phase I studies and one Phase II study with single or multiple dose without an intervention or during endoscopy of the upper gastrointestinal tract or the colon. The generated data indicate a good tolerability of CNS 7056. The effect of CNS 7056 can be reversed by the benzodiazepine antagonist Flumazenil.

A rapid onset and offset of the sedative effect was observed during the procedures. It was also shown that it is possible to achieve the same (safety) or better (efficacy) results as compared to a single dose of the gold standard Midazolam with a single dose of CNS 7056. Furthermore, an adequate sedation level can be maintained for 30 minutes. This time period is usually required to perform a colonoscopy if an additional intervention is required (e. g. removal of one or more polyps). A routine, purely diagnostic colonoscopy takes approximately 10-15 minutes.

The clinically relevant improvement over the gold standard now has to be confirmed in larger trials. Based on the results of the concluded studies, a Phase IIb study with patients undergoing a colonoscopy will be conducted in 2010. The aim of this study is to further refine the optimal dose regimen for Phase III with a multi-centre trial. The preparation of the study has been completed during the first quarter 2010. After having completed the regulatory process in April 2010 the patient enrolment will start shortly. Approximately nine months are scheduled for the patient enrolment phase.

Cooperation Agreements

In 2007 Ono Pharmaceutical Co., Ltd. was granted the rights to develop and market CNS 7056 for the Japanese market in return for development milestone payments and royalties. In February 2010 Ono informed PAION about the initiation of the first Japanese Phase I study. The first subject was enrolled in April 2010 after the balance sheet date. This triggered the first milestone payment of USD 1 million from Ono; payment is expected in May 2010.

Ono is developing CNS 7056 in indications, where continuous infusion is needed, whereas PAION primarily concentrates on indications requiring single or repeat bolus dosing to sedate for short procedures. In this co-operation data are fully shared such that each party benefits from the development progress of the other party.

PAION is exploring partnering opportunities outside Japan to advance the development of CNS 7056, preferably for multiple indications, as quickly as possible as well as to prepare the subsequent commercialisation.

Morphine-6-glucuronide

Morphine-6-glucuronide (M6G), a highly potent opiate, demonstrated in clinical Phase II and Phase III studies a strong analgesic effect in the treatment of moderate to severe, peri-operative pain. At the same time common opiate side effects, such as nausea and vomiting, were significantly reduced with M6G.

Clinical development

Since the acquisition of the project in 2008, PAION has performed various in-depth analyses of the available clinical data. The results support PAION's view that M6G has a wider therapeutic window than morphine at equi-analgesic dosages with a lower incidence of post-operative nausea and vomiting. Based on these findings, in the third quarter of 2009, PAION met with the FDA in order to receive advice on the outstanding clinical development programme. This provided a confirmation of PAION's development proposals to a great extent. The adaptations recommended by the FDA will not impact the projected timelines. The aim of the remaining Phase III programme is to prove that M6G causes significantly less post-operative nausea and vomiting compared to equi-analgesic doses of morphine. Production of the study medication required for the further development was completed during the third quarter 2009. Despite its chemical similarity to morphine, the FDA also confirmed that M6G is regarded as a New Chemical Entity, i.e. a novel, distinct substance. This improves the potential profitability for potential pharma partners as it provides the prospect for longer market exclusivity.

Cooperation Agreements

Based on the results of the in-depth re-analysis and the encouraging FDA consultation PAION continues the search for a development partner for M6G, which is targeted to be concluded in 2010.

Desmoteplase

Desmoteplase is a recombinant protein (a so-called plasminogen activator) derived from the saliva of the vampire bat, *Desmodus rotundus*, which is intravenously administered to dissolve blood clots. It is currently being developed for the treatment of acute ischaemic stroke. The treatment is being carried out in a timeframe of three to nine hours post onset of stroke symptoms – a time window for which there is no approved drug treatment currently.

Clinical Development

So far Desmoteplase has been tested in two Phase II studies and one Phase III study for the treatment of acute ischaemic stroke. In 2008 PAION's license partner Lundbeck took on the further development of Desmoteplase. In December 2008 Lundbeck initiated a further Phase III development programme consisting of two comparable studies (DIAS-3 and DIAS-4). Lundbeck announced in March 2010 that initial patient recruitment in these studies was slower than anticipated. Additional centres will be initiated over the next six months and other initiatives will be taken to speed up recruitment. Therefore, it is only expected to have limited impact on the previously communicated timelines. Lundbeck is expecting a study completion in the second half of 2011. If the studies are positive, Desmoteplase could be eligible for priority review by the FDA.

In 2009 Lundbeck successfully performed a Phase I study in healthy Japanese volunteers. In March 2010 Lundbeck initiated a Phase II study in Japan (DIAS-J).

Cooperation Agreements

PAION in-licensed Desmoteplase from Bayer Schering AG (former Schering AG) in 2001 for milestones and royalties. Under the licence agreement, which came into effect in January 2008, H. Lundbeck A/S has acquired exclusive global rights to develop and market Desmoteplase. Under this agreement, Lundbeck agreed to undertake the following payments:

- Payment of a non-refundable amount of EUR 8 million in advance, on the date the agreement took effect (payment received in January 2008; disclosed as deferred income and being released proportionally over the probable development period),
- Assumption of all future costs, especially for clinical development, production development and marketing approval,
- Milestone payments of up to EUR 63 million, of which up to EUR 38 million relate to milestones due until market approvals (regional splitting) and in total EUR 25 million are due upon commencement of marketing activities and the achievement of specific revenue targets, and
- Payment of licence fees (dependent on revenues) which amount to a low double-digit percentage following the deduction of the licence fees PAION has to pay to the original licensor, Bayer Schering Pharma AG.

PAION has reserved the option to co-promote Desmoteplase in Germany, Austria and Switzerland. If PAION decides to exercise this option it will receive a direct share of earnings rather than licence fees based on revenues.

CNS 5161

After the takeover by PAION in the scope of the CeNeS acquisition in 2008, it was decided to base the further development of CNS 5161 on third-party financing. Such financing could not be secured by year end 2009. The existing development co-operation for CNS 5161 with Ergomed was hence terminated and activities discontinued during the first quarter of 2010. There was no value for CNS 5161 in the balance sheet; therefore the discontinuation of the project does not have any effects on net assets, financial position and results of operations.

Solulin

Solulin is an improved variant of the human protein thrombomodulin, an important natural regulator of blood coagulation. Thrombomodulin is capable of inhibiting the activity and formation of thrombin, an endogenous substance which, when produced in excess, can lead to blood clots. In contrast to natural thrombomodulin, which is an integral protein of vascular membranes, Solulin can travel through the blood stream to reach its potential site of action. Animal models demonstrated that Solulin effectively inhibits the formation of blood clots in veins and arteries.

In 2008 PAION published the results of a clinical Phase I study which involved single and multiple administrations of Solulin. The study confirmed the substance's good safety profile as well as its anticoagulant mode of action offering good potential to inhibit the activity and formation of thrombin.

After availability of the Phase I study results in 2008 PAION offered Solulin to potential partners. The out-licensing discussions with various interested parties however could not be completed successfully. As a result it was decided during the first quarter 2010 to complete the ongoing set of preclinical investigations, which may provide positive data to support further partnering activities. Until these data are available, partnering activities will be put on hold.

Flovagatran

Flovagatran is a substance characterised by a very fast onset of anticoagulation but also very rapid deactivation once intravenous administration is stopped. This is a complementary mode of action to Solulin with an equally fast onset but longer lasting effect. Flovagatran could prove useful as an acute anticoagulant during major surgery such as coronary artery bypass grafting. The substance was previously tested by its originator in two smaller Phase II studies, although in other indications. Therefore PAION is conducting additional preclinical studies in preparation of the clinical assessment of Flovagatran for the reduction of blood loss during cardiac bypass surgery. These studies were started in 2009. Technical difficulties resulted in a delay until the second half of 2010.

Glial Growth Factor (GGF2)

The substance GGF2 (Glial Growth Factor 2) is known to stimulate the growth and differentiation of a variety of cells including glial cells, the support cells of the nervous system. These glial cells form the myelin sheath that insulates nerve cells and is essential for their survival and proper functioning. In demyelinating diseases such as multiple sclerosis, the myelin sheath is damaged, leading to the degeneration of nerve cells. Pre-clinical studies performed by PAION's license partner Acorda have demonstrated that GGF2 can stimulate the cell growth necessary to protect and regenerate a damaged myelin sheath. GGF2 is the lead neuregulin in Acorda's portfolio. Neuregulins have also shown the ability to restore cardiac function in preclinical models of heart failure caused by myocardial infarction, rapid pacing, viral and chemically induced cardiomyopathies. Acorda has filed an IND application with the FDA for GGF2 in March 2010 for the indication of heart failure and intends to perform a Phase I study during the course of 2010.

Cooperation Agreements

The rights relating to the recombinant GGF2, rhGGF2, were licensed to Acorda Therapeutics, Inc. in 2002 by PAION UK (former CeNeS). In March 2010, Acorda filed an IND (Investigational New Drug) application for the substance GGF2. This triggered the obligation to pay the first milestone of USD 0.5 million; the payment was received in April 2010. On 20 April Acorda announced the IND acceptance which triggered the obligation to pay the second milestone of USD 0.5 million; the payment is expected in May 2010. In total, further milestone payments of USD 2.5 million are due prior to market approval and an additional milestone payment of USD 5 million is due upon market authorization; after that PAION will receive revenue dependent royalties.

Net Assets, Financial Position, and Results of Operations

Results of Operations

The loss for the first quarter of 2010 amounted to KEUR -2,871 meaning a decrease of KEUR 456 compared to the prior-year period. The decrease is mainly due to higher revenues because of the achievement of a milestone by Acorda; the payment was received according to plan after the balance sheet date. Research and development expenses as well as administrative expenses decreased slightly compared to the prior-year period. The financial result decreased compared to the previous year on the back of lower money market interest rates as well as lower cash and cash equivalents.

	Q1 2010 KEUR	Q1 2009 KEUR
Revenues	742	405
Cost of revenues	-7	-28
Gross profit	735	377
Research and development expenses	-2,483	-2,616
General and administrative expenses	-1,103	-1,152
Other income (expenses)	15	9
Operating expenses	-3,571	-3,759
Operating result	-2,836	-3,382
Financial result	-135	-26
Income taxes	100	81
Result for the period	-2,871	-3,327

Revenues of KEUR 742 in the first three months of 2010 relate in the amount of KEUR 365 (KUSD 500) to a milestone payment from Acorda for the completion of preclinical preparations for the clinical development of the compound GGF2. Furthermore the revenues include the systematic release of deferred income in connection with the license agreement concluded with Lundbeck (KEUR 364) as well as the refund of development expenses by Lundbeck.

The cost of revenues incurred in the first quarter of 2010 related as well as in the first quarter 2009 to the development expenses incurred in this period, which were refunded by Lundbeck.

Research and development expenses of KEUR 2,483 in the first three months of 2010 decreased slightly by KEUR 133 compared with the corresponding prior-year period. The main research and development focus was on CNS 7056.

General and administrative expenses remained at the prior-year period level in the first quarter of 2010, amounting to KEUR 1,103 (prior-year period: KEUR 1,152).

The financial result for the first three months of 2010 decreased year on year by KEUR 109 down to KEUR -135. The main reasons for the decrease are significantly lower money market interest rates as well as the reduction in cash and cash equivalents compared to the prior-year period.

The income taxes are attributable to tax claims for reimbursement of parts of the research and development costs from the British tax authorities.

Net Assets and Financial Position

The total assets as of 31 March 2010 decreased by KEUR 3,415 compared to 31 December 2009 and amounted to KEUR 32,135. The decrease was mainly due to a lower equity through the loss of the period and lower cash and cash equivalents. As of 31 March 2010 the equity ratio is 51.4%, which means a decline compared to 31 December 2009 (54.3%). If the subordinate loan and the deferred non-refundable upfront payment from Lundbeck were recognised as economic equity, the equity ratio would increase to 87.4%.

	31 March 2010	31 Dec. 2009	Change
	KEUR	KEUR	KEUR
Non-current assets	11,423	11,671	-248
Current assets	20,712	23,879	-3,167
Total assets	32,135	35,550	-3,415
Equity	16,503	19,304	-2,801
Non-current liabilities	11,637	12,033	-396
Current liabilities	3,995	4,213	-218
Total equity and liabilities	32,135	35,550	-3,415

The non-current assets mainly comprise the capitalised development projects of PAION UK Ltd (KEUR 10,825).

The KEUR 3,167 decrease in current assets is mainly attributable to the decrease in cash and cash equivalents (KEUR 3,634). Because of the achievement of a milestone in the development of GGF2 by Acorda the trade receivables increased by KEUR 331 compared to 31 December 2009. The change in cash and cash equivalents stems from the following areas:

	Q1 2010 KEUR	Q1 2009 KEUR
Cash flows from operating activities	-3,480	-3,573
Cash flows from investing activities	-12	-25
Cash flow from financing activities	-146	-164
Effects of exchange rate changes	4	48
Change in cash and cash equivalents	-3,634	-3,714

The negative cash flows from operating activities of KEUR 3,480 were mainly due to the loss of the period in the amount of KEUR 2,871.

The negative cash flows from financing activities in the first three months of 2010 and the prior-year period resulted from interest payments for the subordinated loan raised in April 2006.

The decrease of KEUR 396 in non-current liabilities is attributable to the proportionate release of the deferred income in connection with the license agreement concluded with Lundbeck.

The decrease of KEUR 218 in current liabilities is mainly attributable to the decrease of bonus accruals as well as the decrease of other liabilities.

Personnel Development

On average, PAION employed 29 employees in the first three months of 2010 (fiscal year 2009: 30 employees).

Equity Facility

In May 2010 PAION entered into an equity facility agreement for EUR 15 million with Commerce Court Small Cap Value Fund Ltd. (CCSCVF) managed by Acqua Capital Management Inc., Toronto, Canada. This share facility has a term of 36 months and gives PAION the right to issue new shares out of the existing authorised capital in multiple tranches to CCSCVF against a cash contribution.

CCSCVF has committed to buy these shares at a price calculated based on a daily volume weighted average share price over a five day period (pricing period) less a discount of 5%. CCSCVF guarantees a minimum investment amount per tranche within a range from EUR 150,000 to EUR 1,300,000 dependent on the share price (within a range from EUR 1.00 to and exceeding EUR 8.00). Both parties can agree on higher amounts per tranche. Furthermore PAION has the right to determine for every tranche a floor price below which PAION is not obliged to issue shares. After the end of the pricing period PAION will announce on its website the number of subscribed shares as well as the achieved placement price.

CCSCVF has agreed that during the term of and for a period of 90 days after the termination of the Purchase Agreement, neither CCSCVF nor any of its affiliates will, directly or indirectly, sell, or enter into a short position with respect to any of PAION's shares, except the shares that it owns or has the right to purchase pursuant to the provisions of a draw down notice.

Currently PAION is able to use up to 2,460,291 shares out of its authorized capital for this financing. This facility in the first instance will strengthen PAION's cash position and extend its cash reach. PAION intends to use the cash inflows from this agreement to fund research and development activities, the acquisition (direct or licence) of new development candidates as well as to cover administration expenses.

Risks and Opportunities

Material risks and opportunities relating to future development are presented in detail in the group management report for fiscal year 2009 and have not changed significantly in the first quarter of 2010.

Significant Events Occurring After the Balance Sheet Date

On 3 April 2010 Ono dosed the first subject in a Phase I study with CNS 7056 in Japan. This triggers a milestone of USD 1.0 million. The receipt of the payment is expected in May 2010.

On 20 April 2010 PAION received the first milestone payment of USD 0.5 million from Acorda for the development of GGF2.

On 20 April 2010 PAION's licence partner Acorda announced that the FDA accepted the IND application for GGF2 in the indication of heart failure. This approval triggers the second milestone of USD 0.5 million. The receipt of the payment is expected in May 2010.

On 27 April 2010 PAION reported that it reached agreement with FDA on Phase IIb study design for CNS 7056 in patients undergoing colonoscopy.

On 10 May 2010 PAION entered into an equity facility agreement for EUR 15 million with Commerce Court Small Cap Value Fund Ltd. (CCSCVF) managed by Acqua Capital Management Inc., Toronto, Canada.

Outlook

The equity facility and the milestone payments for development progress from our partners strongly improve PAION's financial situation.

PAION will shortly start a clinical Phase IIb study with CNS 7056. PAION aims to have the compound ready for the clinical Phase III programme in 2011 and expects that the Phase IIb data will enhance the value of CNS 7056 for potential partners. For M6G it is intended to close a partnering agreement in 2010. Beyond that, PAION expects in 2010 extensive development activities by the partners Lundbeck, Ono and Acorda, which could trigger further milestone payments from 2011 onwards.

PAION's research and development expenses in 2010 relate mainly to production development and a clinical Phase IIb study with CNS 7056 in patients undergoing a colonoscopy. The patient enrolment for the Phase IIb study is expected to last approximately nine months. For the other projects in development only minor expenses are planned.

In parallel to PAION's development of CNS 7056 our development partner Ono has started the first clinical Phase I study in Japan with CNS 7056 for the induction and maintenance of anaesthesia, which triggered the first milestone payment of USD 1 million in the beginning of the second quarter 2010. PAION participates from the progress of Ono's development in the form of additional data and financially in the form of milestone payments and royalties from launch onwards.

Our licence partner Lundbeck is currently conducting two worldwide Phase III studies with Desmoteplase in acute ischaemic stroke. Lundbeck expects study completion in 2011 and to be able to file for market approval (MAA/NDA) in 2012. In parallel Lundbeck has started in the first quarter of 2010 a Phase II study with Desmoteplase in stroke in Japan. Lundbeck bears all development costs and pays to PAION milestones up to EUR 63 million and from market entry a double-digit percentage revenue share.

Acorda, our licence partner in the development of GGF2, expects to start the first clinical study by the middle of 2010. In case of further positive development, additional milestone payments of up to USD 7.5 million until approval and afterwards revenue dependent licence fees are payable to PAION.

Revenues in 2010 will include, just as last year, the monthly release of deferred income in connection with the non-refundable milestone payment in the amount of EUR 8 million received from Lundbeck as well as the first milestone payments from the development progress with CNS 7056 and GGF2 of USD 2 million in total. Furthermore PAION expects additional revenues from the intended partnering agreement for M6G.

The budgeted expenses lead, after deduction of the revenues from the existing license agreements with Ono and Acorda, to a significant net loss for the year. The expected revenues from the intended licensing of M6G can significantly reduce the net loss for the year.

As of 31 March 2010 PAION's cash and cash equivalents amounted to EUR 19 million. These plus the milestone payments from Acorda and Ono in 2010 and the expected cash inflows from a partial use of the equity facility secure, based on the current cost structure including the Phase IIb study with CNS 7056, a cash reach until the middle of 2012. This does not account for further upfront payments, milestone payments and cost reimbursements from existing and future partners or an extensive or total use of the equity facility, which could expand the cash reach but may also be used fully or in part for funding of additional development activities within the existing portfolio or newly acquired substances. The cooperation with Lundbeck alone provides for future milestone payments of up to EUR 63 million, of which up to EUR 38 million will become due prior to market approvals.

Aachen, Germany, 11 May 2010

PAION AG



Dr Wolfgang Söhngen



Bernhard Hofer



Dr Mariola Söhngen



Dr Gavin Kilpatrick

Consolidated Balance Sheet

ASSETS	31 March 2010 EUR	31 Dec. 2009 EUR
Non-current assets		
Intangible assets	11,147,223.38	11,379,527.52
Equipment	275,768.11	291,559.18
Other assets	2.25	2.25
	11,422,993.74	11,671,088.95
Current assets		
Trade receivables	424,878.64	94,296.78
Prepaid expenses and other assets	1,049,001.66	913,168.21
Cash and cash equivalents	19,237,693.54	22,871,407.20
	20,711,573.84	23,878,872.19
Total assets	32,134,567.58	35,549,961.14

EQUITY AND LIABILITIES	31 March 2010 EUR	31 Dec. 2009 EUR
Equity		
Share capital	24,602,919.00	24,602,919.00
Capital reserve	88,727,075.23	88,639,947.78
Translation reserve	-1,510,457.37	-1,492,295.41
Loss carryforward	-92,446,174.58	-79,409,073.92
Loss for the period	-2,870,857.03	-13,037,100.66
	16,502,505.25	19,304,396.79
Non-current liabilities		
Provisions	1,428,729.03	1,466,747.40
Financial liabilities	6,866,163.00	6,857,666.84
Deferred income	3,342,171.74	3,708,585.88
	11,637,063.77	12,033,000.12
Current liabilities		
Trade payables	1,675,764.02	1,724,137.09
Provisions	526,481.98	611,381.10
Other current liabilities	313,576.16	391,412.96
Current portion of deferred income	1,479,176.40	1,485,633.08
	3,994,998.56	4,212,564.23
Total equity and liabilities	32,134,567.58	35,549,961.14

Consolidated Statement of Comprehensive Income

EUR	1 January – 31 March 2010	1 January – 31 March 2009
Revenues	741,879.92	404,950.72
Cost of revenues	-7,155.36	-28,032.99
Gross profit	734,724.56	376,917.73
Research and development expenses		
General and administrative expenses	-2,482,699.31	-2,616,189.81
Other income (expenses), net	-1,103,084.24	-1,152,119.92
Operating expenses	15,381.64	8,984.66
	-3,570,401.91	-3,759,325.07
Operating result	-2,835,677.35	-3,382,407.34
Financial income	21,562.06	171,087.14
Financial expenses	-156,619.40	-196,773.60
Financial result	-135,057.34	-25,686.46
Loss for the period before taxes	-2,970,734.69	-3,408,093.80
Income taxes	99,877.66	80,960.17
Loss for the period	-2,870,857.03	-3,327,133.63
of which attributable to other shareholders	0.00	0.00
of which attributable to shareholders of PAION AG	-2,870,857.03	-3,327,133.63
Foreign currency translation of subsidiaries	-18,161.96	332,223.59
Other comprehensive income	-18,161.96	332,223.59
Total comprehensive income	-2,889,018.99	-2,994,910.04
of which attributable to other shareholders	0.00	0.00
of which attributable to shareholders of PAION AG	-2,889,018.99	-2,994,910.04
Earnings per share (basic)	-0.12	-0.14
Earnings per share (diluted)	-0.12	-0.14

Consolidated Cash Flow Statement

EUR	1 January – 31 March 2010	1 January – 31 March 2009
Cash flows from operating activities:		
Net result for the period	-2,870,857.03	-3,327,133.63
Reconciliation of net profit (loss) for the period to cash flows from operating activities:		
Amortization/depreciation and non-cash exchange rate changes of fixed assets	260,180.44	-97,005.11
Interest expenses and interest income	135,057.33	25,686.46
Release of deferred income	-372,870.82	-377,369.76
Expenses from stock option plans	87,127.45	63,345.82
Change in assets and liabilities which are not attributable to investing or financing activities:		
Trade receivables	-330,581.86	55,911.87
Prepaid expenses and other assets	-137,779.26	68,845.31
Trade payables	-48,369.67	-137,065.26
Provisions	-125,267.21	-338,506.07
Other current liabilities	-77,836.44	51,361.99
Deferred income	0.00	36,816.30
Non-cash exchange losses/gains	-22,005.50	283,748.25
Interest received	23,505.40	118,412.14
Net cash used in operating activities	-3,479,706.15	-3,572,951.69
Cash flows from investing activities:		
Cash paid for investments in intangible assets and equipment	-12,085.23	-24,884.81
Net cash used in investing activities	-12,085.23	-24,884.81
Cash flows from financing activities:		
Interest paid	-145,757.68	-145,555.89
Payment of finance lease liabilities	0.00	-18,856.00
Net cash used in financing activities	-145,757.68	-164,411.89
Change in cash and cash equivalents	-3,637,549.06	-3,762,248.39
Effect of exchange rate changes on cash	3,835.40	48,476.38
Cash and cash equivalents at beginning of the period	22,871,407.20	36,071,890.73
Cash and cash equivalents at end of the period	19,237,693.54	32,358,118.72
Composition of cash and cash equivalents at the end of the period:		
Cash	19,237,693.54	32,358,118.72

Consolidated Statement of Changes in Equity

EUR	Share capital	Capital reserve	Translation reserve	Loss carryforward	Equity
31 December 2008	24,602,919.00	88,511,062.55	-2,177,128.79	-79,409,073.92	31,527,778.84
Total comprehensive income	0.00	0.00	332,223.59	-3,327,133.63	-2,994,910.04
Additional contribution to the capital reserve due to the issue of options	0.00	63,345.82	0.00	0.00	63,345.82
31 March 2009	24,602,919.00	88,574,408.37	-1,844,905.20	-82,736,207.55	28,596,214.62
Total comprehensive income	0.00	0.00	352,609.79	-9,709,967.03	-9,357,357.24
Additional contribution to the capital reserve due to the issue of options	0.00	65,539.41	0.00	0.00	65,539.41
31 December 2009	24,602,919.00	88,639,947.78	-1,492,295.41	-92,446,174.58	19,304,396.79
Total comprehensive income	0.00	0.00	-18,161.96	-2,870,857.03	-2,889,018.99
Additional contribution to the capital reserve due to the issue of options	0.00	87,127.45	0.00	0.00	87,127.45
31 March 2010	24,602,919.00	88,727,075.23	-1,510,457.37	-95,317,031.61	16,502,505.25

Selected Explanatory Notes to the Consolidated Interim Financial Statements as of 31 March 2010

General

The quarterly report of PAION AG includes interim consolidated financial statements and an interim group management report in accordance with the provisions of Secs. 37x (3) and 37w (2) to (4) WpHG [“Wertpapierhandelsgesetz”: German Securities Trading Act] in conjunction with Sec. 37y WpHG. The consolidated financial statements were prepared in accordance with the provisions of the International Financial Reporting Standards (IFRSs) for interim financial reporting. The interim group management report was prepared in accordance with the relevant provisions of the German Securities Trading Act.

The interim consolidated financial statements comprise PAION AG as the parent company, registered at Martinstrasse 10-12, 52062 Aachen, Germany, and the wholly-owned subsidiaries, which are fully consolidated:

- PAION Deutschland GmbH, Aachen/Germany
- PAION Holdings UK Ltd, Cambridge/UK
- PAION UK Ltd, Cambridge/UK
- CeNeS Drug Delivery Ltd, Cambridge/UK
- TheraSci Limited, Cambridge/UK
- CeNeS Pharmaceuticals Inc., Norwood/USA
- CeNeS (Bermuda) Ltd, Bermuda

Basis of Accounting

The interim consolidated financial statements have been prepared in accordance with Sec. 315a HGB [“Handelsgesetzbuch”: German Commercial Code] and IFRSs, as adopted by the EU, and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC). All IFRSs issued by the International Accounting Standards Board (IASB), London, UK, which were effective as of the balance sheet date of 31 March 2010 and applied by PAION, were adopted by the European Commission for application in the EU.

The provisions of IAS 34, “Interim Financial Reporting”, have been applied. The interim financial statements as of 31 March 2010 should be read in conjunction with the consolidated financial statements as of 31 December 2009.

The preparation of interim consolidated financial statements in accordance with IFRSs requires management to make estimates and assumptions which have an effect on the amount of recognised assets and liabilities, income and expenses and contingent liabilities. Actual amounts may differ from these estimates.

The estimations and discretionary valuations made in the course of preparing the interim consolidated financial statements apply primarily to the measurement of intangible assets and provisions. The development projects that were capitalised following the acquisition of the PAION UK Group are being written off over a useful life of 14.5 years based on forward-looking assumptions in respect of the time at which regulatory approval is obtained and the patent protection of the products. The provision for long-term leased, unused premises is based on estimated costs incurring up to the end of the contract term.

The interim consolidated financial statements do not contain any segment information as no material reportable segments could be identified.

Consolidation Principles

The consolidation principles used in the interim consolidated financial statements as of 31 March 2010 were the same as those used in the consolidated financial statements as of 31 December 2009.

Foreign Currency Translation

The consolidated financial statements are shown in Euro, which is the functional currency of PAION AG and the reporting currency of the Group. Each company within the Group defines its own functional currency. This is the Euro in the case of the German companies, whereas the UK-based companies use Pound Sterling as their functional currency. All items on the respective financial statements of each company are initially converted to the functional currency at the exchange rate applicable on the transaction date. Monetary

assets and liabilities denominated in a foreign currency are converted to the functional currency on the reporting date at the exchange rate applicable on that date. All ensuing currency differences are recognised in profit or loss with the exception of exchange rate gains and losses from intra-Group loans classified in accordance with IAS 21 as net investments in foreign business operations; these are recognised in equity.

The assets and liabilities of the foreign companies are converted to Euro on the balance sheet reporting date at the exchange rate applicable on that date. These include any and all goodwill in connection with the acquisition of a foreign company and any and all fair value adjustments to the book values of the foreign company's assets and liabilities. Equity components are converted to Euro at historical rates at the time of initial consolidation. Expenses and income are converted to Euro at average monthly exchange rates. The resulting currency differences are accounted for separately within equity.

Accounting Policies

The accounting policies used in the interim consolidated financial statements as of 31 March 2010 were the same as those used in the consolidated financial statements as of 31 December 2009 except for the changes resulting from the revision of IAS 1.

Tax Effects on the Other Comprehensive Income

Because of the negative results of the PAION Group and the existing tax losses carried forward no income taxes are being paid at the moment. In the reporting period the Other Comprehensive Income (foreign currency translation of foreign subsidiaries) does not have any tax effects.

Related Parties

The relationships with related parties have not changed in comparison to those applied in the consolidated financial statements as of 31 December 2009.

Significant Events Occurring After the Balance Sheet Date

On 3 April 2010 Ono dosed the first subject in a Phase I study with CNS 7056 in Japan. This triggers a milestone of USD 1.0 million. The receipt of the payment is expected in May 2010.

On 20 April 2010 PAION received the first milestone payment of USD 0.5 million from Acorda for the development of GGF2.

On 20 April 2010 PAION's licence partner Acorda announced that the FDA accepted the IND application for GGF2 in the indication of heart failure. This approval triggers the second milestone of USD 0.5 million. The receipt of the payment is expected in May 2010.

On 27 April 2010 PAION reported that it reached agreement with FDA on Phase IIb study design for CNS 7056 in patients undergoing colonoscopy.

On 10 May 2010 PAION entered into an equity facility agreement for eur 15 million with Commerce Court Small Cap Value Fund Ltd. (CCSCVF) managed by Acqua Capital Management Inc., Toronto, Canada.

Aachen, Germany, 11 May 2010

PAION AG

Dr Wolfgang Söhngen

Bernhard Hofer

Dr Mariola Söhngen

Dr Gavin Kilpatrick

Review Report

To PAION AG, Aachen:

We have reviewed the interim condensed consolidated financial statements, comprising the balance sheet, statement of comprehensive income, cash flow statement, statement of changes in equity and selected explanatory notes, and the interim group management report of PAION AG, Aachen, for the period from January 1, 2010 to March 31, 2010 which are part of the quarterly financial report pursuant to SEC 37x (3) WpHG ["Wertpapierhandelsgesetz": German Securities Trading Act]. The preparation of the interim condensed consolidated financial statements in accordance with the IFRSs on interim financial reporting as adopted by the EU and of the group management report in accordance with the requirements of the WpHG ["Wertpapierhandelsgesetz": German Securities Trading Act] applicable to interim group management reports is the responsibility of the Company's Management. Our responsibility is to issue a report on the interim condensed consolidated financial statements and the interim group management report based on our review.

We conducted our review of the interim condensed consolidated financial statements and the interim group management report in accordance with German generally accepted standards for the review of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW) and additionally in accordance with the International Standard on Review Engagements "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" (ISRE 2410). Those standards require that we plan and perform the review to obtain a certain level of assurance in our critical appraisal to preclude that the interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IFRSs on interim financial reporting as adopted by the EU and that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the WpHG. A review is limited primarily to making inquiries of company personnel and applying analytical procedures and thus does not provide the assurance that we would obtain from an audit of financial statements. In accordance with our engagement, we have not performed a financial statement audit and, accordingly, we do not express an audit opinion.

Based on our review nothing has come to our attention that causes us to believe that the interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IFRSs on interim financial reporting as adopted by the EU and that the interim group management report has not been prepared, in all material respects, in accordance with the provisions of the WpHG applicable to interim group management reports.

Cologne, Germany, 11 May 2010
Ernst & Young GmbH
Wirtschaftsprüfungsgesellschaft

(s) Gockel	(s) Zwirner
Wirtschaftsprüfer	Wirtschaftsprüfer
[German Public Auditor]	[German Public Auditor]

PAION AG

Martinstrasse 10-12

52062 Aachen Germany

Phone +49-241-4453-0

Fax +49 241 4453-100

info@paion.com www.paion.com