

PAION Q3#2010

Consolidated Financial Interim Report for the Third Quarter 2010
and the Nine-Month Period ending 30 September 2010

Contents

Interim Group Management Report for the Nine-Month Period ending 30 September 2010	3
Overview	3
Share Performance	4
Overview of Research and Development Activities	5
Net Assets, Financial Position, and Results of Operations	10
Personnel Development	12
Changes in the Supervisory Board	12
Equity Facility	12
Risks and Opportunities	13
Significant Events Occurring After the Balance Sheet Date	13
Outlook	14
Consolidated Balance Sheet	18
Consolidated Statement of Comprehensive Income	20
Consolidated Cash Flow Statement	21
Consolidated Statement of Changes in Equity	22
Selected Explanatory Notes to the Consolidated Interim Financial Statements as of 30 September 2010	23
Review Report	26

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PAION AG

Key Figures

(all figures in KEUR unless otherwise noted)	Q3 2010	Q3 2009	Q1-Q3 2010	Q1-Q3 2009
Revenues	368	377	2,604	1,164
Research and development expenses	-2,226	-2,783	-6,579	-8,275
General administrative and selling expenses	-1,082	-1,121	-3,312	-3,388
Net result for the period	-2,992	-3,152	-7,319	-10,043
Earnings per share in EUR for the period (basic)	-0.12	-0.13	-0.30	-0.41
Earnings per share in EUR for the period (diluted)	-0.12	-0.13	-0.30	-0.41

	Q1-Q3 2010	Q1-Q3 2009
Cash flows from operating activities	-7,390	-8,828
Cash flows from investing activities	-21	-53
Cash flows from financing activities	-442	-498
Average number of group employees	29	30

	30 Sept. 2010	31 Dec. 2009
Intangible assets	10,999	11,380
Cash and cash equivalents	15,033	22,871
Equity	12,579	19,304
Non-current liabilities	10,826	12,033
Balance sheet total	27,390	35,550
Equity ratio	45.9%	54.3%

Interim Group Management Report for the Nine-Month Period ending 30 September 2010

Overview

- PAION starts Phase IIb study with Remimazolam/CNS 7056 (May 2010)
- PAION receives milestone payments from partners (April/May 2010)
- PAION substantially strengthens its financial position with an equity facility and milestone payments, extending its cash reach until the middle of 2012 (May 2010)
- PAION completes Phase IIb study with Remimazolam/CNS 7056 (September 2010)
- PAION expands Desmoteplase agreement with Lundbeck (October 2010)
- Revenues more than doubled
- Net loss reduced by 27%

The first nine months of 2010 were marked by the conduct of the Phase IIb study with Remimazolam/CNS 7056; the last patient was enrolled in September. Furthermore important milestones were reached such as the initiation of the first Phase I trial of Remimazolam/CNS 7056 in Japan by PAION 's development partner Ono Pharmaceutical in April 2010, which triggered the first milestone payment of EUR 0.7 million and the IND (Investigational New Drug) application filed by our licensee Acorda Therapeutics for the substance GGF2, which triggered milestone payments of a total of EUR 0.7 million.

On 27 September 2010 the completion of the Phase IIb clinical trial, assessing the new short-acting intravenous anesthetic/sedative Remimazolam/CNS 7056 in patients undergoing colonoscopy was announced. No drug-related Serious Adverse Event has been reported. The recruitment for the Phase IIb trial was completed in only four months. Headline data are expected by the end of November 2010.

On 15 October 2010 PAION announced the expansion of the Desmoteplase agreement with Lundbeck. Lundbeck gets access to potential follow-up compounds and receives research rights. Conversely PAION receives payments of up to EUR 31.5 million, thereof:

- An upfront payment of EUR 1.5 million, which was received in October and will be recognised as revenue in the fourth quarter 2010.
- EUR 5 million increase of Desmoteplase milestone payments to a total of up to EUR 68 million.
- Up to EUR 25 million milestone payments for development and commercialisation of the second generation molecules (follow-up compounds).

In addition to the clinical milestones, an important step to strengthen the financial position of the company was to enter 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. In November PAION has utilised EUR 0.8 million out of the equity facility against new shares. The equity facility is described in more detail on page 12 under “Equity Facility”.

Compared to the prior-year period, revenues increased by EUR 1.4 million to EUR 2.6 million, mainly due to the milestones from Ono and Acorda. Research and development expenses decreased by EUR 1.7 million compared to the prior-year period. The loss for the first nine months of 2010 of EUR -7.3 million was EUR 2.7 million lower than in the corresponding prior-year period (EUR -10.0 million). Cash and cash equivalents decreased by EUR 7.8 million in the first nine months of 2010 to EUR 15.0 million.

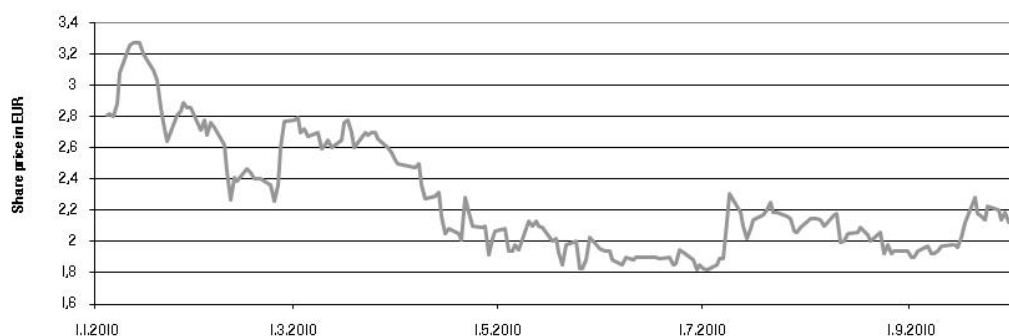
PAION 's cash and cash equivalents of EUR 15 million as of 30 September 2010 and the expected cash inflows from a partial use of the equity facility secure, based on the current cost structure, a cash reach until the middle of 2012.

Share Performance

The PAION share started into the year 2010 at a price of EUR 2.81 (Xetra) and reached on 12 January 2010 a closing price of EUR 3.27 (Xetra), marking a new peak price since October 2007. Thereafter the share price decreased steadily, reaching the lowest point for the first nine months of 2010 on 29 June 2010 at EUR 1.82 (Xetra). Supported by positive news flow as well as positive expectations from the financial press an increase of the share price at the end of the third Quarter could be observed. The closing price on 30 September 2010 was EUR 2.12 (Xetra). This corresponds to a decrease of 17% compared to the closing price of 2009 (EUR 2.55; Xetra). The benchmark index DAXsubsector Biotechnology Index lost 13% in the first nine month of 2010.

The overall average daily trading volume (Xetra, Frankfurt Stock Exchange resp. all German Stock Exchanges) amounted to 62,333 shares during the first nine months of 2010 (in the year 2009: 61,410 shares). Thereby 12.0 million shares (49% of total shares) were traded during the first nine months of 2010 (in the year 2009: 15.5 million shares and 63% of total shares respectively).

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



Overview of Research and Development Activities

Remimazolam (INN)/ CNS 7056

The international nonproprietary name (INN) for the compound CNS 7056 given by the World Health Organisation is Remimazolam.

Remimazolam/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 Remimazolam/CNS 7056 rapidly induces the desired sedation. Importantly, for the benefit of the patient, this sedative effect quickly disappears again. This means 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. Remimazolam/CNS 7056 is currently being developed by PAION as a sedative agent for day case procedures. It has additional potential in the induction and maintenance of anaesthesia, which is the initial indication being developed by our partner Ono for the Japanese market. Furthermore, Remimazolam/CNS 7056 could also be used as a sedative during artificial respiration in the Intensive Care Unit (ICU).

Clinical Development

The clinical studies performed with Remimazolam/CNS 7056 comprise two Phase I and two Phase II studies 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 Remimazolam / CNS 7056. The effect of Remimazolam/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 Remimazolam/CNS 7056. Furthermore, an adequate sedation level can be maintained for 30 minutes with a multiple dose regimen. 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.

Based on the results of the concluded studies, a Phase IIb study with patients undergoing a colonoscopy was 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 patient recruitment was initiated in May 2010 and completed by the end of September 2010. It is expected that headline data will be available by end of November 2010.

Cooperation Agreements

In 2007 Ono Pharmaceutical Co., Ltd. was granted the rights to develop and market Remimazolam/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. This triggered the first milestone payment of USD 1 million from Ono.

Ono is developing Remimazolam/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 continually exchanged so that each party benefits from the development progress of the other party.

PAION is exploring partnering opportunities outside Japan to advance the development of Remimazolam/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, PAION met with the FDA in 2009 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 end of 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

Despite the positive results of the in-depth re-analysis and the encouraging FDA consultation PAION has so far not been able to conclude a global partnership. Currently PAION is in discussions on continuing the development together with several partners.

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 licence 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 November 2010 that the phase III studies for Desmoteplase in ischaemic stroke, DIAS-3 and DIAS-4, is ongoing and is expected to be filed by the end of 2012. Additional centres will be opened and other initiatives have begun in order to speed up recruitment. Desmoteplase could be eligible for priority review by the FDA. 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 and was extended in September 2010, H. Lundbeck A/S holds the exclusive global rights to develop and market Desmoteplase and potential follow-up compounds. Under these agreements, 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 (January 2008; disclosed as deferred income and being released proportionally over the probable development period),
- Payment of a non-refundable amount of EUR 1.5 million in advance, on the date the extended agreement took effect (October 2010 and will be recognised as revenue in the fourth quarter 2010),
- Milestone payments for Desmoteplase of up to EUR 68 million, of which up to EUR 40 million relate to milestones due until market approvals (regional splitting) and in total EUR 28 million are due upon commencement of marketing activities and the achievement of specific revenue targets,
- Milestone payments for the second generation molecules (follow-up compounds) of up to EUR 25 million for development and commercialisation,
- Assumption of all costs, especially for clinical development, production development, patent costs and marketing approval,
- 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 did 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.

So far Solulin has been tested clinically in a 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 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 in new indications to support further partnering activities. Until these data are available, partnering activities have been 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. The final data is expected by the end of the year.

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. In pre-clinical studies PAION's licence partner Acorda 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. In April 2010 the FDA approved the IND (Investigational New Drug) application for GGF2 for the indication of heart failure. In July 2010 Acorda announced that the National Heart, Lung, and Blood Institute (NHLBI) has awarded a USD 1 million Cardiac Translational Research Implementation Program (C-TRIP) grant to Acorda and its collaborator Vanderbilt University Heart and Vascular Institute to support the early phase clinical research on GGF2. Acorda and Vanderbilt intend to start a Phase I study.

Cooperation Agreements

The rights relating to the recombinant GGF2, rh GGF2, were licensed to Acorda Therapeutics, Inc. in 2002 by PAION UK. The IND application submitted in March 2010 triggered the obligation to pay the first milestone of USD 0.5 million; the payment was received in April 2010. The IND approval communicated by Acorda in April 2010 triggered the obligation to pay the second milestone of USD 0.5 million; the payment was received in May 2010. In total, further milestone payments of USD 2.5 million prior to market approval and an additional milestone payment of USD 5 million are due upon market authorization; after that PAION will receive revenue dependent royalties.

Net Assets, Financial Position, and Results of Operations

Results of Operations

Revenues increased by KEUR 1,440 compared to the prior-year period, which is mainly due to the milestone payments from Ono (KEUR 749) and Acorda (KEUR 737).

Research and development expenses decreased by KEUR 1,696 compared to the prior-year period.

General administrative and selling expenses remained at the prior-year period level.

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.

The loss for the first nine months of 2010 amounted to KEUR -7,319; a decrease of KEUR 2,724 compared to the prior-year period. The decrease is mainly due to higher revenues and lower research and development expenses.

	Q3 2010	Q3 2009	Q1-Q3 2010	Q1-Q3 2009
	KEUR	KEUR	KEUR	KEUR
Revenues	368	377	2,604	1,164
Cost of revenues	-2	-9	-15	-48
Gross profit	366	368	2,589	1,116
Research and development	-2,226	-2,783	-6,579	-8,275
General administrative and selling	-1,082	-1,121	-3,312	-3,388
Other income (expenses)	-28	431	70	519
Operating expenses	-3,336	-3,473	-9,821	-11,144
Operating result	-2,970	-3,105	-7,232	-10,028
Financial result	-141	-131	-416	-270
Taxes on income	119	84	329	255
Net result for the period	-2,992	-3,152	-7,319	-10,043

Revenues in the first nine months of 2010 relate in the amount of KEUR 749 (USD 1 million) to a milestone payment from Ono for the start of the Phase I study with Remimazolam/CNS 7056 in Japan and in the amount of KEUR 737 (USD 1 million) to two milestone payments from Acorda of USD 0.5 million each for the submission and subsequent approval of the IND for the compound GGF2. Furthermore the revenues include the systematic release of deferred income in connection with the licence agreement concluded with Lundbeck (KEUR 1,091) as well as the refund of development expenses by Lundbeck.

Research and development expenses of KEUR 6,579 in the first nine months of 2010 decreased by KEUR 1,696 compared with the corresponding prior-year period. The main research and development focus was on Remimazolam/CNS 7056.

General administrative and selling expenses remained at the prior-year period level in the first nine months of 2010, amounting to KEUR 3,312 (prior-year period: KEUR 3,388).

The **financial result** for the first nine months of 2010 decreased year on year by KEUR 146 to KEUR -416. 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 30 September 2010 decreased by KEUR 8,160 compared to 31 December 2009 and amounted to KEUR 27,390. The decrease was mainly due to a lower equity through the loss of the period and lower cash and cash equivalents. As of 30 September 2010 the equity ratio is 45.9%, 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 be 85.7%.

	30 Sept. 2010	31 Dec. 2009	Change
	KEUR	KEUR	KEUR
Non-current assets	11,187	11,671	-484
Current assets	16,203	23,879	-7,676
Total Assets	27,390	35,550	-8,160
Equity	12,579	19,304	-6,725
Non-current liabilities	10,826	12,033	-1,207
Current liabilities	3,985	4,213	-228
Total Equity and liabilities	27,390	35,550	-8,160

The **non-current assets** mainly comprise the capitalised development projects of PAION UK Ltd (KEUR 10,696).

The KEUR 7,676 decrease in **current assets** is mainly attributable to the decrease in cash and cash equivalents (KEUR 7,838). The change in cash and cash equivalents stems from the following areas:

	Q1-Q3 2010 KEUR	Q1-Q3 2009 KEUR
Cash flows from operating activities	-7,390	-8,828
Cash flows from investing activities	-21	-53
Cash flow from financing activities	-442	-498
Effects of exchange rate changes	15	61
Change in cash and cash equivalents	-7,838	-9,318

The negative cash flows from operating activities of KEUR 7,390 were mainly due to the loss of the period in the amount of KEUR 7,319. The negative cash flows from operating activities were KEUR 1,438 lower than in the prior-year period. This is mainly due to the milestone payments from Ono and Acorda.

The negative cash flows from financing activities in the first nine months of 2010 and the prior-year period resulted in the amount of KEUR 442 from interest payments for the subordinated loan raised in April 2006.

The decrease of KEUR 1,207 in **non-current liabilities** is attributable to the proportionate release of the deferred income in connection with the licence agreement concluded with Lundbeck.

The decrease of KEUR 228 in **current liabilities** is mainly attributable to lower trade payables.

Personnel Development

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

Changes in the Supervisory Board

The Annual General Meeting on 19 May 2010 re-elected Dr Wenninger as member of the Supervisory Board. Afterwards the Supervisory Board elected Dr Spiekerkötter as Chairman of the Supervisory Board and Dr Wenninger as Deputy Chairman of the Supervisory Board.

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 until May 2013 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, enter into a short position with respect to any of PAION's shares, except the shares that it has the right to purchase pursuant to the provisions of a draw down notice.

In November 2010 300,000 shares were issued at a price of EUR 2.5287 leading to a cash inflow of EUR 758,610.

Currently PAION is able to use up to 2,160,291 shares out of its authorised 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 strengthen its cash position as well as to fund research and development activities, for 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 nine months of 2010.

Significant Events Occurring After the Balance Sheet Date

On 15 October 2010 PAION announced the expansion of the Desmoteplase agreement with Lundbeck. Lundbeck gets access to potential follow-up compounds and receives research rights. Conversely PAION receives payments of up to EUR 31.5 million, thereof:

- An upfront payment of EUR 1.5 million, which was received in October and will be recognised as revenue in the fourth quarter 2010.
- EUR 5 million increase of Desmoteplase milestone payments to a total of up to EUR 68 million.
- Up to EUR 25 million milestone payments for development and commercialisation of the second generation molecules (follow-up compounds).

Outlook

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

PAION completed the clinical Phase IIb study with Remimazolam/CNS 7056 in September 2010 and expects headline data by the end of November 2010. PAION expects that the Phase IIb study results will enhance the value of Remimazolam for potential partners. After the availability of the Phase IIb data paion will continue the Remimazolam partnering discussions with vigour. In parallel, PAION will continue the ongoing talks with several potential partners regarding M6G. Beyond that, paion expects 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 the completed clinical Phase IIb study with Remimazolam/CNS 7056. For the other projects in development only minor expenses are incurred.

In parallel to PAION's development of Remimazolam/CNS 7056 our development partner Ono has started the first clinical Phase I study in Japan with Remimazolam/CNS 7056 for the induction and maintenance of anaesthesia, which triggered the first milestone payment of EUR 0.7 million. 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 to be able to file for market approval (MAA/NDA) end of 2012. In parallel in the first quarter of 2010 Lundbeck started a Phase II study with Desmoteplase in stroke in Japanese patients. Lundbeck bears all development costs and pays to PAION milestones up to EUR 68 million and from market entry a double-digit percentage revenue share.

Acorda, our licence partner in the development of GGF2, plans as the next step the start of the first clinical study. 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 include the monthly release of deferred income in connection with the non-refundable milestone payment in the amount of EUR 8 million received from Lundbeck in 2008 as well as the milestone payments already received from the development progress with Remimazolam/CNS 7056 and GGF2 of EUR 1.5 million in total. In October PAION has generated revenues of EUR 1.5 million from the extended agreement with Lundbeck.

The budgeted expenses lead, after deduction of the revenues from the existing licence agreements with Lundbeck, Ono and Acorda to a significant net loss for the year.

As of 30 September 2010 PAION's cash and cash equivalents amounted to EUR 15 million. In October 2010 PAION received EUR 1.5 million from Lundbeck and in November a total of EUR 0.8 million from a capital increase. The cash and cash equivalents 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 Remimazolam/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. These 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 68 million, of which up to EUR 40 million will become due prior to market approvals.

Aachen, Germany, 10 November 2010

PAION AG



Dr. Wolfgang Söhngen



Bernhard Hofer



Dr. Mariola Söhngen



Dr. Gavin Kilpatrick

Consolidated Interim Financial Statements

PAION AG

Consolidated Balance Sheet

ASSETS	30 Sept. 2010 EUR	31 Dec. 2009 EUR
Non-current assets		
Intangible assets	10,999,025.67	11,379,527.52
Equipment	188,498.22	291,559.18
Other assets	2.32	2.25
	11,187,526.21	11,671,088.95
Current assets		
Trade receivables	3,200.95	94,296.78
Prepaid expenses and other assets	1,166,298.58	913,168.21
Cash and cash equivalents	15,033,311.56	22,871,407.20
	16,202,811.09	23,878,872.19
Total assets	27,390,337.30	35,549,961.14

EQUITY AND LIABILITIES	30 Sept. 2010 EUR	31 Dec. 2009 EUR
Equity		
Share capital	24,602,919.00	24,602,919.00
Capital reserve	88,914,969.60	88,639,947.78
Translation reserve	-1,173,375.23	-1,492,295.41
Loss carryforward	-92,446,174.58	-79,409,073.92
Loss for the period	-7,319,372.25	-13,037,100.66
	12,578,966.54	19,304,396.79
Non-current liabilities		
Provisions	1,332,638.65	1,466,747.40
Finance liabilities	6,884,087.19	6,857,666.84
Deferred income	2,609,343.46	3,708,585.88
	10,826,069.30	12,033,000.12
Current liabilities		
Trade payables	1,400,980.75	1,724,137.09
Provisions	827,694.29	611,381.10
Other current liabilities	290,969.86	391,412.96
Current portion of deferred income	1,465,656.56	1,485,633.08
	3,985,301.46	4,212,564.23
Total equity and liabilities	27,390,337.30	35,549,961.14

Consolidated Statement of Comprehensive Income

EUR	1 July – 30 Sept. 2010	1 July – 30 Sept. 2009	1 January – 30 Sept. 2010	1 January – 30 Sept. 2009
Revenues	368,304.14	376,565.59	2,603,713.48	1,164,106.49
Cost of revenues	-1,827.31	-8,862.55	-14,865.50	-48,600.95
Gross profit	366,476.83	367,703.04	2,588,847.98	1,115,505.54
Research and development expenses	-2,226,134.39	-2,782,759.94	-6,578,949.82	-8,274,937.40
General administrative and selling expenses	-1,081,809.01	-1,120,793.95	-3,312,399.85	-3,388,124.29
Other income (expenses), net	-28,662.05	430,652.29	69,877.39	519,315.59
Operating expenses	-3,336,605.45	-3,472,901.60	-9,821,472.28	-11,143,746.10
Operating result	-2,970,128.62	-3,105,198.56	-7,232,624.30	-10,028,240.56
Financial income	17,752.92	60,276.22	56,187.49	312,879.01
Financial expenses	-158,732.12	-191,595.14	-471,881.90	-582,627.94
Financial result	-140,979.20	-131,318.92	-415,694.41	-269,748.93
Loss for the period before taxes	-3,111,107.82	-3,236,517.48	-7,648,318.71	-10,297,989.49
Income taxes	118,781.88	84,593.26	328,946.46	254,824.52
Loss for the period	-2,992,325.94	-3,151,924.22	-7,319,372.25	-10,043,164.97
of which attributable to other shareholders	0.00	0.00	0.00	0.00
of which attributable to shareholders of PAION	-2,992,325.94	-3,151,924.22	-7,319,372.25	-10,043,164.97
Foreign currency translation of subsidiaries	-496,179.86	-730,771.58	318,920.18	491,988.96
Other comprehensive income	-496,179.86	-730,771.58	318,920.18	491,988.96
Total comprehensive income	-3,488,505.80	-3,882,695.80	-7,000,452.07	-9,551,176.01
of which attributable to other shareholders	0.00	0.00	0.00	0.00
of which attributable to shareholders of PAION AG	-3,488,505.80	-3,882,695.80	-7,000,452.07	-9,551,176.01
Earnings per share (basic)	-0.12	-0.13	-0.30	-0.41
Earnings per share (diluted)	-0.12	-0.13	-0.30	-0.41

Consolidated Cash Flow Statement

EUR	1 January – 30 Sept. 2010	1 January – 30 Sept. 2009
Cash flows from operating activities:		
Net result for the period	-7,319,372.25	-10,043,164.97
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	445,729.09	220,712.78
Loss/Profits from the disposal of non-current assets	58,677.21	15,148.86
Interest expenses and interest income	415,694.38	269,748.93
Release of deferred income	-1,119,218.94	-1,123,134.26
Expenses from stock option plans	275,021.82	109,556.91
Change in assets and liabilities which are not attributable to investing or financing activities:		
Trade receivables	91,095.83	76,894.42
Prepaid expenses and other assets	-613,637.10	44,975.76
Trade payables	-323,158.93	270,660.38
Provisions	78,648.44	-13,847.53
Other current liabilities	-100,443.39	-110,905.98
Deferred income	0.00	49,184.04
Non-cash exchange losses/gains	303,865.62	430,649.46
	-7,807,098.22	-9,803,521.20
Interest received	52,045.27	288,139.06
Tax payments received	364,651.44	686,959.55
Net cash used in operating activities	-7,390,401.51	-8,828,422.59
Cash flows from investing activities:		
Cash paid for investments in intangible assets and equipment	-20,843.56	-52,443.89
Net cash used in investing activities	-20,843.56	-52,443.89
Cash flows from financing activities:		
Interest paid	-441,912.34	-441,801.78
Payment of finance lease liabilities	0.00	-56,568.00
Net cash used in financing activities	-441,912.34	-498,369.78
Change in cash and cash equivalents	-7,853,157.41	-9,379,236.26
Effect of exchange rate changes on cash	15,061.77	61,337.43
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	15,033,311.56	26,753,991.90
Composition of cash and cash equivalents at the end of the period:		
Cash and cash equivalents	15,033,311.56	26,753,991.90

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	491,988.96	-10,043,164.97	-9,551,176.01
Additional contribution to the capital reserve due to the issue of options	0.00	109,556.91	0.00	0.00	109,556.91
30 September 2009	24,602,919.00	88,620,619.46	-1,685,139.83	-89,452,238.89	22,086,159.74
Total comprehensive income	0.00	0.00	192,844.42	-2,993,935.69	-2,801,091.27
Additional contribution to the capital reserve due to the issue of options	0.00	19,328.32	0.00	0.00	19,328.32
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	318,920.18	-7,319,372.25	-7,000,452.07
Additional contribution to the capital reserve due to the issue of options	0.00	275,021.82	0.00	0.00	275,021.82
30 September 2010	24,602,919.00	88,914,969.06	-1,173,375.23	-99,765,546.83	12,578,966.54

Selected Explanatory Notes to the Consolidated Interim Financial Statements as of 30 September 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

The wholly owned subsidiary CeNeS (Bermuda) Ltd, Bermuda, was dissolved on 2 July 2010 and is no longer consolidated. The derecognition does not have any effects on the Group’s net assets, financial position and results of operations.

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

30 September 2010 and applied by PAION, were adopted by the European Commission for application in the EU.

The following new announcements were published by the IASB during the reporting period and will be applied as soon as they come into effect if at that point an adoption by the European Commission has taken place.

- In May 2010 the IASB published the collective standard “Annual Improvements 2010”, which implements minor changes to the existing IFRS. The standard contains amendments to eight standards (IFRS/IAS) and one interpretation (IFRIC). The majority of the amendments must be applied to fiscal years commencing on or after 1 January 2011.
- In October 2010 the IASB published amendments to IFRS 7 “Financial Instruments: Disclosures”. The amendments relate to extended disclosures regarding the transfer of financial assets and shall allow users of financial statements to improve their understanding of the possible effects of any risks that may remain with the entity that transferred the assets. The amendments are effective for fiscal years beginning on or after 1 July 2011; earlier application would be permitted. In the first year of application comparative disclosures are not required. The amendments could result in additional disclosure obligations in future financial statements. The amendments do not have any effects on the Group’s net assets, financial position and results of operations.
- In October 2010 the IASB published additions to IFRS 9 „Financial Instruments: Recognition and Measurement“. The existing IFRS 9 (2009) published in November 2009 prescribed only the classification and measurement of financial assets. In addition the now published IFRS 9 (2010) includes rules regarding the classification and measurement of financial liabilities as well as rules regarding the derecognition of financial assets and financial liabilities. IFRS 9 is effective for fiscal years beginning on or after 1 January 2013. The additions do not have any effects on the Group’s net assets, financial position and results of operations.

The provisions of IAS 34, "Interim Financial Reporting", have been applied. The interim financial statements as of 30 September 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 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 30 September 2010 were the same as those used in the consolidated financial statements as of 31 December 2009.

Foreign Currency Translation

The interim 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 30 September 2010 were the same as those used in the consolidated financial statements as of 31 December 2009.

Tax Effects on 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.

Earnings per Share

Potential ordinary shares from the exercise of stock options are dilutive only if the new ordinary shares from the exercise of stock options would increase the loss per share. Because of the negative results of the PAION Group there is currently no dilution from potential new ordinary shares from the stock option programmes.

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.

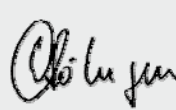
Significant Events Occurring After the Balance Sheet Date

On 15 October 2010 PAION announced the expansion of the Desmoteplase agreement with Lundbeck. Lundbeck gets access to potential follow-up compounds and receives research rights. Conversely PAION receives payments of up to EUR 31.5 million, thereof:

- An upfront payment of EUR 1.5 million, which was received in October and will be recognised as revenue in the fourth quarter 2010.
- EUR 5 million increase of Desmoteplase milestone payments to a total of up to EUR 68 million.
- Up to EUR 25 million milestone payments for development and commercialisation of the second generation molecules (follow-up compounds).

Aachen, Germany, 10 November 2010

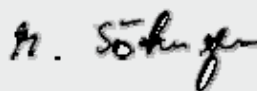
PAION AG



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 September 30, 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, 10 November 2010

Ernst & Young GmbH

Wirtschaftsprüfungsgesellschaft

(s) Gockel

Wirtschaftsprüfer

[German Public Auditor]

(s) Zwirner

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