

PALATIN TECHNOLOGIES INC  
Form PREM14A  
July 13, 2004

[PALATIN LOGO OMITTED]

**PALATIN TECHNOLOGIES, INC.**  
**4C Cedar Brook Drive**  
**Cranbury, New Jersey 08512**

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**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**

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DATE Friday, August 27, 2004

TIME 9:30 a.m., Eastern Time

PLACE Palatin's executive offices, 4C Cedar Brook Drive, Cranbury, New Jersey 08512

RECORD DATE July 13, 2004

ITEMS OF BUSINESS(1) approval of an amendment to the Certificate of Incorporation to increase the authorized common stock;  
(2) approval of an increase in common stock available for issuance under the 1996 Stock Option Plan; and  
(3) any other matters properly brought before the meeting.

STOCKHOLDER LIST A list of all stockholders entitled to vote at the meeting will be available for examination by any stockholder, for any purpose germane to the meeting, during ordinary business hours for 10 days before the meeting, at our executive offices, 4C Cedar Brook Drive, Cranbury, New Jersey 08512.

By order of the board of directors,

Stephen T. Wills, *Secretary*  
July \_\_, 2004

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**PALATIN TECHNOLOGIES, INC.**

**SPECIAL MEETING 2004**

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**PALATIN TECHNOLOGIES, INC.**

**SPECIAL MEETING 2004**

## PROXY STATEMENT

### VOTING PROCEDURES AND SOLICITATION

#### YOUR VOTE IS IMPORTANT

Whether or not you plan to attend the meeting, please complete and return the enclosed proxy card. Your prompt voting may save us the expense of following up with a second mailing. We began sending out these proxy materials on approximately July \_\_, 2004.

#### METHODS OF VOTING

You may vote by signing and returning the enclosed proxy card or by voting in person at the meeting. If you send in a proxy card, and also attend the meeting in person, the proxy holders will vote your shares as you instructed on your proxy card, unless you inform the Secretary at the meeting that you wish to vote in person.

#### REVOKING A PROXY

You may revoke your proxy by:

signing and returning another proxy card at a later date;

sending written notice of revocation to the Secretary at our offices, 4C Cedar Brook Drive, Cranbury, New Jersey 08512; or

informing the Secretary and voting in person at the meeting.

To be effective, a later-dated proxy or written revocation must arrive at our corporate offices before the start of the meeting.

#### PROXY SOLICITATION

We are soliciting the enclosed proxy card on behalf of the board of directors, and we will pay all costs of preparing, assembling and mailing the proxy materials. In addition to mailing out proxy materials, our officers and employees may solicit proxies by telephone or fax, without receiving any additional compensation for their services. We have requested brokers, banks and other fiduciaries to forward proxy materials to the beneficial owners of our stock.

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#### HOW PROXY CARDS ARE VOTED

The proxy holders named on the proxy card are Carl Spana, Ph.D., chief executive officer, president and a director, and Stephen T. Wills, chief financial officer, executive vice president, secretary and treasurer. The proxy holders will vote shares according to the stockholder's instructions on the proxy card. If a signed proxy card does not contain instructions, then the proxy holders will vote the shares FOR the approval of the amendment to the Certificate of Incorporation increasing authorized common stock; FOR approval of the increase in common stock available for issuance under the 1996 Stock Option Plan; and in their discretion on any other business which may properly come before the meeting.

## QUORUM AND VOTES REQUIRED

A majority of the votes of outstanding shares of common stock and Series A preferred stock, represented at the meeting in person or by proxy, constitutes a quorum. Abstentions and broker non-votes will count towards the quorum. A broker non-vote occurs when a nominee holding shares for a beneficial owner does not vote on a particular proposal because the nominee does not have discretionary voting power for that particular item, and has not received instructions from the beneficial owner. Common stock and Series A preferred stock will vote together as one class on the two items of business listed on the proxy card.

approval of the amendment to the Certificate of Incorporation increasing authorized common stock requires the affirmative vote of a majority of all outstanding stock. Abstentions and broker non-votes will count against approval.

approval of the increase in common stock available for issuance under the 1996 Stock Option Plan requires a majority of the votes cast. Abstentions and broker non-votes will count neither for nor against the proposal.

## VOTING RIGHTS, SHARES OUTSTANDING AND VOTES PER SHARE

Holders of common stock and of Series A preferred stock at the close of business on the record date of July 13, 2004 are entitled to vote at the meeting.

Common stock: 52,790,900 shares outstanding, one vote per share

Series A preferred stock: 11,697 shares outstanding, approximately 38.02 votes per share, a total of 444,739 votes

## ITEM ONE: INCREASE IN AUTHORIZED COMMON STOCK

*The proposed amendment.* Under our Certificate of Incorporation, Palatin is authorized to issue up to 75,000,000 shares of common stock and 10,000,000 shares of preferred stock. On June 10, 2004, the board of directors adopted, subject to stockholder approval, an amendment to the Certificate of Incorporation which would increase the authorized common stock to 150,000,000 shares. The amendment would not affect the authorized preferred stock.

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*Outstanding and reserved shares.* Of the 75,000,000 shares of common stock currently authorized, the following amounts are outstanding or reserved as of July 13, 2004:

52,790,900	outstanding
444,752	reserved for issuance on conversion of outstanding preferred stock
8,026,425	reserved for issuance on conversion of outstanding warrants
4,445,609	reserved for issuance on conversion of outstanding options
<u>275,956</u>	reserved for future option grants under the 1996 Stock Option Plan
65,983,642	total outstanding and reserved

We therefore have only 9,016,358 shares of common stock available for future use. The board has determined that this amount is insufficient to allow us to continue funding our operations, compensating our management, employees and consultants, engaging in strategic business alliances and joint ventures, and otherwise for pursuing our business objectives and long-term goals.

*Purpose for the increase.* Since acquiring our core business in a merger in 1996, we have issued stock and derivative securities for the following purposes:

raising equity capital to fund our ongoing operations;

compensating the placement agents in our private offerings;

issuing convertible preferred stock as equity participation in a strategic corporate alliance;

issuing warrants as part of the consideration for contracts such as technology licensing, property leasing and financial consulting; and

providing incentive and compensatory stock options to management, employees, and consultants. If the stockholders approve the increase in the shares of common stock available for issuance under the 1996 Stock Option Plan, as discussed under Item 2 below, we will reserve an additional 5,000,000 shares for this purpose.

We expect to continue issuing common stock, and securities convertible into or exercisable for common stock, for these purposes. In addition, the board may consider issuing securities in connection with business acquisitions, alliances and joint ventures, other business opportunities, employee benefit plans other than our existing stock option plan, stock dividends, stock splits and other general corporate purposes. The board has the discretion, without further stockholder approval, to authorize new series of preferred stock and set the terms of the preferred stock, including conversion into common stock, for which the board may reserve any portion of the available common stock. See the Description of Securities below.

*Effect of the increase on rights of existing security holders.* The proposed amendment will not affect the rights of existing security holders. See the Description of Securities below.

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*Anti-takeover effect.* Increasing the authorized common stock could enhance the board's power to influence any change of control. The board has the authority, without further approval of the stockholders, to issue and determine

the rights and preferences of other series of preferred stock, except as limited by the certificate of designation for the Series A stock. The board could issue one or more series of preferred stock with voting, conversion, dividend, liquidation, or other rights which would adversely affect the voting power and ownership interest of holders of common stock. This authority may have the effect of deterring hostile takeovers, delaying or preventing a change in control, and discouraging bids for our common stock at a premium over the market price.

**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR THE ITEM 1 PROPOSAL, TO APPROVE THE AMENDMENT TO THE CERTIFICATE OF INCORPORATION TO INCREASE THE AUTHORIZED COMMON STOCK.**

## DESCRIPTION OF SECURITIES

### Common Stock

We have authority to issue 75,000,000 shares of common stock, par value \$0.01 per share. As of July 13, 2004, 52,790,900 shares of our common stock were outstanding, and a maximum of 12,392,034 shares of common stock were issuable on conversion of outstanding convertible preferred stock or exercise of outstanding options and warrants. Holders of common stock have one vote per share and have no preemption rights. Holders of common stock have the right to participate ratably in all distributions, whether of dividends or assets in liquidation, dissolution or winding up, subject to any superior rights of holders of preferred stock outstanding at the time. See Description of Preferred Stock and Series A Convertible Preferred Stock, below.

*Stock Exchange Listing.* Our common stock is listed and registered on the American Stock Exchange (AMEX). If the stockholders approve the increase in authorized common stock, we intend to list and register on AMEX all shares of the newly authorized common stock which we subsequently offer for sale or reserve for issuance.

*Transfer Agent and Registrar.* American Stock Transfer & Trust Company is the transfer agent and registrar for our common stock. Their address is 59 Maiden Lane, Plaza Level, New York, NY 10038 and their telephone number is (800) 937-5449.

### Preferred Stock

We have authority to issue 10,000,000 shares of preferred stock. As of July 13, 2004, 11,697 shares of our preferred stock were outstanding (see Series A Convertible Preferred Stock, below). The description of preferred stock provisions set forth below is not complete and is subject to and qualified in its entirety by reference to our certificate of incorporation and the certificate of designations relating to each series of preferred stock.

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The board of directors has the right, without the consent of holders of common stock, to designate and issue one or more series of preferred stock, which may be convertible into common stock at a ratio determined by the board. A series of preferred stock may bear rights superior to common stock as to voting, dividends, redemption, distributions in liquidation, dissolution, or winding up, and other relative rights and preferences. The board may set the following terms of any series preferred stock, and a supplemental prospectus will specify these terms for each series offered:

the number of shares constituting the series and the distinctive designation of the series;

dividend rates, whether dividends are cumulative, and, if so, from what date; and the relative rights of priority of payment of dividends;

voting rights and the terms of the voting rights;

conversion privileges and the terms and conditions of conversion, including provision for adjustment of the conversion rate;

redemption rights and the terms and conditions of redemption, including the date or dates upon or after which shares may be redeemable, and the amount per share payable in case of redemption, which may vary under different conditions and at different redemption dates;

sinking fund provisions for the redemption or purchase of shares;

Trights in the event of voluntary or involuntary liquidation, dissolution or winding up of the corporation, and the relative rights of priority of payment;

any other relative powers, preferences, rights, privileges, qualifications, limitations and restrictions of the series.

Dividends on outstanding shares of preferred stock will be paid or declared and set apart for payment before any dividends may be paid or declared and set apart for payment on the common stock with respect to the same dividend period.

If upon any voluntary or involuntary liquidation, dissolution or winding up of the corporation, the assets available for distribution to holders of preferred stock are insufficient to pay the full preferential amount to which the holders are entitled, then the available assets will be distributed ratably among the shares of all series of preferred stock in accordance with the respective preferential amounts (including unpaid cumulative dividends, if any) payable with respect to each series.

Holders of preferred stock will not be entitled to preemptive rights to purchase or subscribe for any shares of any class of capital stock of the corporation. The preferred stock will, when issued, be fully paid and nonassessable. The rights of the holders of preferred stock will be subordinate to those of our general creditors.

We have previously issued preferred stock in three series, designated Series A Convertible Preferred Stock, Series B Convertible Preferred Stock and Series C Convertible Preferred Stock. All of the issued shares of Series B, issued in 1998, and Series C, issued in 1999, were retired upon conversion into common stock and are no longer outstanding.

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### **Series A Convertible Preferred Stock**

The board of directors established a series of 264,000 shares of preferred stock, designated Series A Convertible Preferred Stock. We issued 137,780 shares of Series A stock in 1997, of which 11,697 shares remain outstanding, the rest having been converted into common stock. The Series A stock has the following rights and preferences.

*Optional conversion.* Each share of Series A stock is convertible at any time, at the option of the holder, into the number of shares of common stock equal to \$100 divided by the conversion price, as defined in the Series A certificate of designations. The current conversion price is \$2.63, so each share of Series A stock is currently convertible into approximately 38 shares of common stock.

*Mandatory conversion.* We may, at our option, cause the conversion of the Series A stock, in whole or in part, on a pro rata basis, into common stock, if the closing bid price of the common stock has exceeded 200% of the conversion price for at least 20 trading days in any 30 consecutive trading day period, ending three days prior to the date of mandatory conversion.

*Price protection provisions.* The conversion price decreases if we sell common stock (or equivalents) for a price per share less than the conversion price or less than the market price of the common stock. The conversion price is also subject to adjustment upon the occurrence of a merger, reorganization, consolidation, reclassification, stock dividend or stock split which results in an increase or decrease in the number of shares of common stock outstanding.

*Dividend and distribution preference.* We may not pay a dividend or make any distribution to holders of any other capital stock unless and until we first pay a special dividend or distribution of \$100 per share to the holders of Series A stock.

*Liquidation Preference.* Upon (i) liquidation, dissolution or winding up of the company, whether voluntary or involuntary, (ii) sale or other disposition of all or substantially all of the assets of the company, or (iii) any consolidation, merger, combination, reorganization or other transaction in which Palatin is not the surviving entity or in which the shares of common stock constituting in excess of 50% of the voting power of the company are exchanged for or changed into other stock or securities, cash and/or any other property, after payment or provision for payment of the debts and other liabilities of the company, the holders of Series A stock will be entitled to receive, pro rata and in preference to the holders of any other capital stock, an amount per share equal to \$100 plus accrued but unpaid dividends, if any.

*Voting rights.* Each holder of Series A stock has the number of votes equal to the number of shares of common stock issuable upon conversion of the holder's Series A stock at the record date for determination of the stockholders entitled to vote or, if no record date is established, at the date a vote is taken. Except as provided above or as required by applicable law, the holders of the Series A stock will be entitled to vote together with the holders of the common stock and not as a separate class.

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## **Securities Authorized for Issuance under Equity Compensation Plans**

We have issued options and warrants as equity compensation under various plans, including the 1996 Stock Option Plan described under Item 2 below. The following table shows the outstanding options and warrants as of June 30, 2004 under all equity compensation plans. The table does not include new options granted to officers and directors on July 1, 2004 (see Interest of Management In Share Increase under Item 2 below). The table also does not include warrants which we have sold to investors to raise equity capital.

### **EQUITY COMPENSATION PLAN INFORMATION AS OF JUNE 30, 2004**



<u>Plan category</u>	Number of securities to be issued upon exercise of outstanding options, warrants and rights (1)	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders (2)	4,755,684	\$3.45	355,956
Equity compensation plans not approved by security holders	1,456,187	\$3.14	0

- (1) Does not include a total of 19 shares of aggregated fractions. No fractional shares will be issued on exercise of options or warrants.
- (2) Includes individual option and warrant agreements we assumed when we merged with RhoMed Incorporated in 1996. Options and warrants to purchase 471,127 shares of common stock are outstanding under the assumed agreements, with a weighted average exercise price of \$2.03 per share. No additional options or warrants are available for issuance, except that the number of shares purchasable under certain warrants may increase due to anti-dilution provisions.

We have authorized the issuance of equity securities under the compensation plans described below, without the approval of stockholders. No additional options, warrants or rights are available for issuance under any of these plans, except for additional shares which may become purchasable under warrants with anti-dilution protection as noted below. We have already registered for resale the common stock underlying all of these options and warrants.

1997 Executive Officers Stock Option Agreement, dated June 3, 1997: provided common stock purchase options to three executive officers. Options to purchase 26,766 shares at \$4.96 per share are outstanding, with an expiration date of June 3, 2007.

Richard J. Murphy Stock Option Agreement, dated December 4, 1997: provided common stock purchase options to a former director to purchase 5,000 shares at \$5.44 per share and 1,066 shares at \$7.50 per share, with an expiration date of December 4, 2007. These options replaced options for the same number of shares at the same prices which terminated under our 1996 Stock Option Plan.

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Watson Laboratories settlement warrants, dated March 15, 2000: provided common stock purchase warrants to eight individuals who participated in a privately negotiated resale of 363,636 shares of our common stock, to purchase an aggregate of 50,000 shares at \$0.01 per share, with an expiration date of March 15, 2005. Warrants to purchase 15,125 shares remain outstanding.

Griffin Financial Services Advisory Agreement warrants, dated June 8, 2000: provided common stock purchase warrants to Griffin Securities, Inc., a financial consultant, to purchase 5,000 shares at \$7.00 per share, with an expiration date of June 8, 2005.

Wistar Institute of Anatomy and Biology warrants, dated December 15, 2000: provided common stock purchase warrants to a technology licensor to purchase 15,000 shares at \$4.00 per share, with an expiration date of December 15, 2010.

Cedar Brook II Corporate Center, L.P. warrants, dated April 6, 2001 and December 17, 2001: provided common stock purchase warrants to the lessor of our office and laboratory facility to purchase 30,000 shares at \$2.90 per share, with an expiration date of April 6, 2006, and 25,000 shares at \$3.65 per share with an expiration date of December 17, 2006.

Wistar Institute of Anatomy and Biology warrants, dated May 13, 2002: provided common stock purchase warrants to a technology licensor to purchase 15,000 shares at \$2.82 per share, with an expiration date of May 15, 2012.

Placement warrants: provided common stock purchase warrants as compensation to various private offering placement agents to purchase an aggregate of 1,318,230 shares. These warrants have the following share amounts, prices (rounded to the nearest cent) and expiration dates:

Offering	Shares Purchasable	Exercise Price	Expiration Date
Fall 2000	216,000	\$6.60	10-05-05
Fall 2000	87,884	\$6.53	10-27-05
Fall 2001	134,188	\$2.66	10-29-06
Fall 2001	221,872	\$2.70	10-29-06
June 2002	109,510	\$2.75	06-13-07
July 2002	51,502	\$1.46	07-29-07
July 2002	38,627	\$1.37	07-29-07
Fall 2002	458,647	\$1.54	11-15-07

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## **ITEM TWO: INCREASE IN SHARES AVAILABLE FOR ISSUANCE UNDER THE 1996 STOCK OPTION PLAN**

The board has authorized an amendment to our 1996 stock option plan to increase in the number of shares of common stock available for issuance under the plan from 5,000,000 shares to 10,000,000 shares. Any increase in the number of shares available under the plan requires stockholder approval. The complete text of the amendment is set forth at the end of this section of the proxy statement. Because of the relatively small amount of authorized common stock remaining available for issuance for any purpose, the board has made this amendment to the stock option plan contingent on stockholder approval of the increase in authorized common stock described in Item 1 above.

As of July 1, 2004, options to purchase 4,290,361 shares were outstanding, and options to purchase 433,683 shares had been exercised. This leaves only 275,956 shares available for grant under the plan. The board believes that our ability to continue providing non-cash compensation and incentives in the form of stock options is crucial to our ability to attract, retain and motivate talented employees, consultants and non-employee directors.

**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR THE ITEM 2 PROPOSAL TO APPROVE THE INCREASE IN COMMON STOCK AVAILABLE FOR ISSUANCE UNDER THE 1996 STOCK OPTION PLAN.**

**THE PLAN**

The 1996 stock option plan, which the stockholders approved in August 1997, is our only active stock option plan. Some options to purchase common stock are still outstanding under other plans, but those plans are not available for granting new options. The 1996 plan will terminate in August 2006. Its purpose is to allow us to provide additional non-cash compensation and incentives, in the form of options to purchase our common stock, to our employees, non-employee directors and consultants.

*Administration and amendment of the plan.* The plan is administered by the compensation committee of the board or by the full board. The board may amend or terminate the plan at any time, except that without stockholder approval, the board may not:

increase the total number of shares available under the plan;

change the manner of determining option prices;

extend the maximum term of options (10 years); or

extend the plan beyond its current expiration date of August 27, 2006.

No termination or amendment of the plan may adversely affect the rights of an option holder without the holder's consent.

*Participants.* Participation in the plan is limited to those employees, non-employee directors and consultants of Palatin or its subsidiaries to whom the compensation committee or board grants options under the plan. We currently have 60 employees, including three executive officers and the chairman of the board, and six non-employee directors, who are eligible to receive options under the plan.

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*Option prices.* Recipients do not pay any consideration for the grant of an option, but will pay us the exercise price for common stock purchasable under an option if and when they choose to exercise the option. The exercise price per share for stock underlying the option is determined at the time of grant and must be at least the market price of common stock on the date of grant. The market price of common stock on July 9, 2004 was \$3.80 per share.

*Option vesting and expiration.* The vesting schedule and expiration date of each option is determined at the time of grant. The maximum period for exercise of any option under the plan is 10 years from the date of grant. Although the plan expires in August 2006, options granted before the plan expires will continue to be exercisable until the expiration date of each individual option. Options may be subject to early termination as described below.

*Exercise.* An option holder may exercise all or any part of the vested portion of an option by delivering written notice to Palatin, along with payment in immediately available U.S. funds of the exercise price for the number of shares specified. An option holder who takes certain distributions (a hardship withdrawal) from a 401(k) plan of Palatin or its subsidiaries will not be able to exercise any option for a period of one year after the distribution.

*Termination.* Unless otherwise provided by the committee or board, if an option holder ceases to serve as an employee, non-employee director or consultant of Palatin or its subsidiaries, whether voluntarily or otherwise, that option holder's non-vested options will terminate immediately, and vested options will terminate on the earlier of 90 days after the option holder leaves employment or service, or the final expiration date of the option. If an option holder's employment or service is terminated for cause (as defined below), then that option holder's outstanding options will terminate immediately. For purposes of the plan, cause means:

the commission by an option holder of any act or omission that would constitute a crime under federal, state or equivalent foreign law;

the commission by an option holder of any act of moral turpitude;

fraud, dishonesty or other acts or omissions that result in a breach of any fiduciary or other material duty to Palatin or its subsidiaries; or

continued alcohol or other substance abuse that renders an option holder incapable of performing his or her material duties to the satisfaction of Palatin or its subsidiaries.

All outstanding options will terminate upon Palatin's dissolution or liquidation, or a merger, reorganization or consolidation in which Palatin is not the surviving corporation, unless otherwise provided in a plan adopted to effect the change in Palatin's corporate status.

*Adjustments.* If we issue a common stock dividend, the number of shares purchasable under each outstanding option will increase to include the number of shares to which the holder would have been entitled to receive as a dividend if the option shares had been outstanding. If we exchange the outstanding common stock for a different number or kind of shares of stock or other securities of Palatin or another corporation, whether through reorganization, recapitalization, stock split, combination of shares, sale of assets, or merger or consolidation in which we are the surviving corporation, then each share of common stock purchasable under outstanding options will become the number and kind of securities for which each outstanding share of common stock has been exchanged.

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*Tax consequences.* Options granted under the plan may be either tax-qualified employee incentive options or non-qualified options. Qualified options can be granted only to employees, while non-qualified options can be granted to employees, non-employee directors, and consultants.

In the case of qualified options, neither grant nor exercise results in compensation income to the employee or a compensation deduction for the company. If the employee holds the stock issued on exercise for a holding period of at least two years after the date of grant, or one year after the exercise (whichever is longer), then upon subsequent sale of the stock, the employee will recognize as capital gains income (not compensation income) the difference between the sale price and the exercise price. If the employee sells the stock before the prescribed holding period has passed (a disqualifying disposition), then the employee will recognize as compensation income the difference between the exercise price and

the fair market value of the stock at the time of exercise. That compensation income will be added to the basis of the option stock in determining the capital gain, if any, on the disqualifying disposition.

In the case of non-qualified options, the grant does not result in compensation income for the option holder or a compensation deduction for the company. The exercise of a non-qualified option results in the option holder recognizing as compensation income the difference between the exercise price and the fair market value of the stock at the time of exercise. The company would have a compensation deduction in the same amount.

*Registration of shares and resale restrictions.* We have registered the common stock currently authorized for issuance under the plan under the Securities Act of 1933 on Form S-8. If the stockholders approve the proposed increase, we intend to register the additional 5,000,000 shares on Form S-8. However, all employees and consultants of Palatin and its subsidiaries must comply with our policy on securities trading, which includes restrictions on purchase and sale of our securities and handling of confidential information. Our securities trading policy restricts resale of common stock to specified window periods, and prohibits resale at any time when the employee or consultant possesses material non-public information about Palatin. Employees are encouraged to consult with our chief financial officer before reselling any common stock, even during a window period. Our securities trading policy does not, however, restrict the purchase of common stock from Palatin upon exercise of an option. Former employees and consultants are not bound by the securities trading policy unless they have so agreed.

*Transfer of options.* An option which is not an incentive stock option, as defined in Section 422(b) of the Internal Revenue Code, may be assigned or transferred to and exercised by a participant's family member as defined in the Securities and Exchange Commission's Form S-8, General Instruction A(5). Transfer of an option for value is permitted only to the extent not prohibited under Form S-8, General Instruction A(5). Otherwise, options or interests in options under the plan are not transferable except by will or the laws of descent and distribution, and options are exercisable only by the option holder during his or her lifetime.

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## OPTIONS GRANTED TO MANAGEMENT AND EMPLOYEES

The following table shows all outstanding options as of July 13, 2004, whether currently exercisable or not, granted under the plan to our officers, directors and employees. This table does not include the options granted on July 1, 2004 to officers and directors which are subject to stockholder approval of the increase in plan shares. Those options will not be exercisable unless and until the stockholders approve the proposed increase in plan shares. See Interest of Management In Share Increase and the New Option Benefits Table below. This table also does not include options to purchase a total of 149,167 shares granted to various consultants.

### OUTSTANDING OPTIONS TABLE - 1996 STOCK OPTION PLAN

Name and Position -----	Number of Option Shares -----
Carl Spana, Ph.D., president, chief executive officer and director(1)	780,000
Stephen T. Wills, MST, CPA, executive vice president and chief financial officer, secretary and treasurer	651,250
Shubh D. Sharma, Ph.D., vice president and chief technical officer(2)	180,000

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John K.A. Prendergast, Ph.D., director and chairman of the board(3)	406,667
Perry B. Molinoff, M.D., director	261,250
Robert K. deVeer, Jr., director	214,440
Zola P. Horovitz, Ph.D., director	105,000
Robert I. Taber, Ph.D., director	100,000
Errol de Souza, Ph.D., director	58,750
THREE EXECUTIVE OFFICERS AS A GROUP:	1,611,250
SIX NON-EXECUTIVE DIRECTORS AS A GROUP:	1,146,107
NON-MANAGEMENT EMPLOYEES AS A GROUP: (4)	1,383,837

- (1) Does not include options to purchase 100,962 shares which Dr. Spana holds under other plans.
- (2) Does not include options to purchase 14,669 shares which Dr. Sharma holds under other plans.
- (3) Includes options granted to Summercloud Bay, Inc., a consulting firm of which Dr. Prendergast is the president and sole stockholder.
- (4) Non-management employees hold options to purchase an aggregate of 3,640 shares granted under other plans.

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**INTEREST OF MANAGEMENT IN SHARE INCREASE**

Effective July 1, 2004, the board granted options for a total of 460,000 shares to executive officers and 50,000 shares to the chairman, as specified in the New Option Benefits Table below. The board granted these options subject to stockholder approval of an increase in the plan shares. The exercise price for all of these options is \$4.21 per share, they vest as to 1/3 of the shares on July 1 of 2004, 2005 and 2006, and they expire 10 years from the date of grant. The dollar value of the options is calculated for purposes of this table on the basis of a market price per share on July 9, 2004 as quoted on AMEX, of \$3.80 per share. None of the options will be exercisable unless and until the stockholders approve the proposed increase in the shares available under the plan.

**NEW OPTION BENEFITS TABLE**

Name and Position -----	Dollar Value -----	Number of Option Sha -----
Carl Spana, Ph.D., president, chief executive officer and director	\$0	200,000
Stephen T. Wills, executive vice president and chief financial officer, secretary and treasurer	\$0	175,000
Shubh D. Sharma, Ph.D., vice president and chief	\$0	85,000

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technical officer

THREE EXECUTIVE OFFICERS AS A GROUP:	\$0	460,00
John K.A. Prendergast, Ph.D., director and chairman	\$0	50,00

In the event that the stockholders do not approve the proposed increase in the shares available under the plan, the new options shown above will terminate. If the stockholders do approve the increase, the options shown above will become effective, and the balance of 4,815,956 shares then available under the plan will be available for further grants to directors and officers, as well as to other employees and consultants.

We have not granted or agreed to grant any options to management other than the outstanding options and the new options granted subject to approval of the increase in plan shares, as shown in the tables above. If the stockholders approve the increase in plan shares, we expect to continue granting options in accordance with our current compensation policies.

*Executive option grants.* Our current employment agreements with executive officers do not require us to grant options. However, our current executive compensation practices include annual bonus compensation, which usually includes option grants to executive officers. The Summary Compensation Table on page 18 shows the amount of options granted to executive officers in fiscal years 2001, 2002 and 2003. During fiscal year ended June 30, 2004, we granted options to our executive officers totaling 230,000 shares. For a description of our current executive compensation practices, see the Compensation Committee Report starting on page 23.

*Grants to chairman.* Dr. Prendergast, the chairman of the board, is also an employee of Palatin, but not an executive officer. Our current employment agreement with Dr. Prendergast does not require us to grant options. In fiscal 2004, we granted an option to Dr. Prendergast for 50,000 shares.

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*Non-employee directors' initial option grants.* When a non-employee director is first elected to the board, he receives an option to purchase an amount of common stock determined by the board, up to 10,000 shares, at the market value on the date of grant. These options vest as to 25% of the option per year, starting on the date of grant. They expire 10 years from the date of grant.

*Non-employee directors' annual option grants.* On December 5, 2003, each non-employee director (Messrs. deVeer, Horovitz, Taber and De Souza) received an option to purchase 10,000 shares of common stock at \$3.16 per share. These options related to compensation for the six-month period from January 1 through June 30, 2004. They vested in six monthly installments, starting on the last day of January, 2004, and expire ten years from the date of grant. Starting July 1, 2004, each non-employee director will receive on July 1 of each year an option to purchase 20,000 shares of common stock at the closing price on June 30. These options vest in 12 monthly installments, starting on the last day of July, and expire ten years from the date of grant. Messrs. deVeer, Horovitz, Taber and De Souza each received an option on July 1, 2004, to purchase 20,000 shares at \$4.51 per share, the closing price on June 30, 2004. The annual option grant does not apply to Dr. Molinoff, with whom we have a consulting agreement.

Management's interest in stockholder approval of an increase in plan shares available includes validation of the options granted to the executive officers and the chairman on July 1, 2004, which are not currently exercisable, and the ability to continue to receive option grants under the plan.

**TEXT OF PLAN AMENDMENT**

Section 3 of the plan will be amended to read as follows (changed language is bracketed and struck through):

3. Stock Subject to Plan.

[~~5,000,000~~] 10,000,000 of the authorized but unissued shares of the Common Stock, \$0.01 par value, of the Company (the Common Stock ) are hereby reserved for issue upon the exercise of Options granted under the Plan; provided, however, that the number of shares so reserved may from time to time be reduced to the extent that a corresponding number of issued and outstanding shares of the Common Stock are purchased by the Company and set aside for issue upon the exercise of Options. If any Options expire or terminate for any reason without having been exercised in full, the unpurchased shares subject thereto shall again be available for the purposes of the Plan.

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**EXECUTIVE OFFICERS**

<u>Name</u>	<u>Age</u>	<u>Position with Palatin</u>
Carl Spana, Ph.D.	41	President, chief executive officer and director
Stephen T. Wills, CPA	47	Executive vice president and chief financial officer, secretary and treasurer
Shubh D. Sharma, Ph.D.	48	Vice president and chief technical officer

Executive officers are appointed by the board and serve at the discretion of the board. Each officer holds his position until his successor is appointed and qualified. All of the current executive officers hold office under employment agreements.

CARL SPANA, Ph.D., co-founder of Palatin, has been our president and chief executive officer since June 14, 2000. He has been a director of Palatin since June 1996 and has been a director of our wholly-owned subsidiary, RhoMed Incorporated, since July 1995. From June 1996 through June 14, 2000, Dr. Spana served as an executive vice president and our chief technical officer. From June 1993 to June 1996, Dr. Spana was vice president of Paramount Capital Investments, LLC, a biotechnology and biopharmaceutical merchant banking firm, and of The Castle Group Ltd., a medical venture capital firm. At Paramount Capital Investments and at Castle Group, Dr. Spana was responsible for discovering, evaluating, and commercializing biotechnologies. Through his work at Paramount Capital Investments and Castle Group, Dr. Spana co-founded and acquired several private biotechnology firms. From July 1991 to June 1993, Dr. Spana was a Research Associate at Bristol-Myers Squibb, a publicly traded pharmaceutical company, where he was involved in scientific research in the field of immunology. Dr. Spana is a director of AVAX Technologies, Inc., a publicly traded medical technology company. Dr. Spana received his Ph.D. in molecular biology from The Johns Hopkins University and his B.S. in biochemistry from Rutgers University.

STEPHEN T. WILLS, CPA, MST, has been a vice president, secretary, treasurer and our chief financial officer since November 1997. From July 1997 to August 2000, Mr. Wills was a vice president and the chief financial officer of Derma Sciences, Inc., a publicly held company which provides wound and skin care products, and currently serves as a director of Derma. From 1991 to August 2000, he was the president and chief operating officer of Golomb, Wills & Company, P.C., a public accounting firm. Mr. Wills, a certified public accountant, received his B.S. in accounting from West Chester University, and an M.S. in taxation from Temple University.



SHUBH D. SHARMA, Ph.D., has been a vice president and chief technical officer since August 1, 2001. He had been our executive director of research since November 2000, and director of chemistry since 1996. He is the inventor of our MIDAS drug design technology platform. Dr. Sharma was associate director of research and development and director of peptide research for RhoMed Incorporated (now our wholly-owned subsidiary) at the time we merged with RhoMed in 1996, and had worked as director of peptide research for RhoMed since 1994. Previously he had worked on drug design and peptide research at the University of Arizona in Tucson, and at the Swiss Federal Institute of Technology in Zurich, Switzerland. Dr. Sharma received his Ph.D. from the Central Drug Research Institute in Lucknow, India.

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EXECUTIVE COMPENSATION

*Summary compensation table.* The following table summarizes the compensation paid to our chief executive officer and the other named executive officers for the last three fiscal years. With respect to the persons and periods covered in the following table, we made no restricted stock awards, have no outstanding stock appreciation rights ( SARs ) and have no long-term incentive plan ( LTIP ).

**SUMMARY COMPENSATION TABLE**

Name and Principal Position	Year	Annual Compensation		Long Term Compensation	All other Compen- sation
		Salary	Bonus	Awards	
				Option Shares (1)	
Carl Spana, Ph.D., chief executive officer	2004	\$320,000	\$50,000 (2a)	100,000	\$3,805 (3)
	2003	\$290,000	\$50,000 (2b)	100,000	\$3,543 (4)
	2002	\$291,042 (5)	--	100,000 (6)	\$58,305 (7)
Stephen T. Wills, CPA, MST, chief financial officer	2004	\$265,000	\$40,000 (2a)	80,000	\$19,107 (8)
	2003	\$225,000	\$40,000 (2b)	80,000	\$18,131 (9)
	2002	\$226,833 (5)	--	70,000 (6)	\$16,472 (10)
Shubh D. Sharma, Ph.D., vice president and chief technical officer	2004	\$185,000	\$23,333 (2a)	50,000	\$19,107 (11)
	2003	\$165,000	\$23,333 (2b)	30,000	\$17,081 (12)
	2002	\$162,083	--	35,000 (5)	\$13,091 (13)

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	Annual Compensation	Long Term Compensation
		Awards

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Name and Principal Position -----	Year ----	Salary -----	Bonus -----	Option Shares (1) -----	All other Compen- sation -----
Perry B. Molinoff, M.D., executive vice president of research & development (14)	2004	\$90,372	\$26,667 (2a)	50,000	\$8,285 (15)
	2003	\$250,000	\$26,667 (2b)	60,000	\$17,665 (16)
	2002	\$205,715	--	--	\$46,192 (17)

(1) The security underlying all options listed is common stock.

(2a) Bonus earned and paid in fiscal year 2004.

(2b) Bonus earned in fiscal year 2003 and paid in fiscal year 2004.

(3) Includes 401(k) matching contributions of \$2,800 and life/disability insurance premiums of \$1,005.

(4) Includes 401(k) matching contributions of \$2,538 and life/disability insurance premiums of \$1,005.

(5) Includes one pay period of retroactive FY 2001 base salary earnings paid in FY 2002.

(6) Options granted in fiscal year 2002 relate to compensation for fiscal year 2001. No options were granted relative to fiscal 2002.

(7) Includes a relocation benefit of \$55,000, 401(k) matching contributions of \$2,300 and life/disability insurance premiums of \$1,005.

(8) Includes health insurance premiums of \$11,952, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$6,150.

(9) Includes health insurance premiums of \$11,126, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$6,000.

(10) Includes health insurance premiums of \$10,248, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$5,219.

(11) Includes health insurance premiums of \$11,952, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$6,150.

(12) Includes health insurance premiums of \$7,089 and 401(k) matching contributions of \$3,075.

(11) Includes health insurance premiums of \$11,126, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$4,950.

(13) Includes health insurance premiums of \$10,248, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$1,838.

(14) Dr. Molinoff resigned as an officer effective November 3, 2003.

(15) Includes health insurance premiums of \$3,639, life/disability insurance premiums of \$355 and 401(k) matching contributions of \$4,311.

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(16) Includes health insurance premiums of \$10,660, life/disability insurance premiums of \$1,005 and 401(k) matching contributions of \$6,000.

(17) Includes a relocation benefit of \$32,809, health insurance premiums of \$8,482, life/disability insurance premiums of \$838 and 401(k) matching contributions of \$4,063.

*Option grants in last fiscal year.* The following table shows options granted to our named executive officers during the fiscal year ended June 30, 2004. All of the options listed were granted under our 1996 stock option plan, and the underlying security is common stock. All options granted in fiscal 2004 vested as to one third of the shares on the date of grant, and will vest as to the remaining two thirds of the shares only upon achievement of performance objectives. The exercise price for each option is equal to the market price of common stock on the date of grant. We have not granted any SARs.

**OPTION GRANTS IN LAST FISCAL YEAR**

INDIVIDUAL GRANTS						Pote
Name	Number of Securities Underlying Options Granted (#)	% of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price (\$/Sh)	Expiration Date		Va An Ap 5
Carl Spana	100,000	17.6%	\$3.24	07/16/2013		\$20
Stephen T. Wills	80,000	14.1%	\$3.24	07/16/2013		\$16
Shubh D. Sharma	50,000	8.8%	\$3.24	07/16/2013		\$10
Perry B. Molinoff	50,000	8.8%	\$3.24	07/16/2013		\$10

\* Potential realizable value is shown in response to SEC rules which require the information, for illustration purposes only. The values shown are not representations or projections of future stock prices or the future value of our common stock.

Aggregated option exercises and fiscal year-end option values. No executive officer exercised any options during the fiscal year ended June 30, 2004. We have not granted any SARs. Fiscal year-end values in the following table are based on the closing price for the common stock, as reported on AMEX on June 30, 2004, of \$4.21 per share.

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**AGGREGATED OPTION EXERCISES  
AND FISCAL YEAR-END OPTION VALUES**

Name	Shares Acquired on Exercise	Value Realized	Shares Underlying Unexercised Options at		Value of
			Fiscal Year 2004 Exercisable	Fiscal Year 2004 Unexercisable	Unexercised In-the-Money Options at Fiscal Year 2004 Exercisable
Carl Spana	0	\$0	797,628	83,334	\$797,876
Stephen T. Wills	0	\$0	584,583	66,667	\$489,941
Shubh D. Sharma	0	\$0	148,032	46,667	\$85,550
Perry B. Molinoff	0	\$0	261,250	0	\$150,650

*Ten-year option repricings.* We did not adjust or amend the exercise price of any stock options during the fiscal year ended June 30, 2004. We have not granted any SARs. The following table shows all option repricings for all executive officers at any time during the last 10 years.

**TEN-YEAR OPTION REPRICINGS**

Name	Date	Number of Securities Underlying Options Repriced or Amended (#)	Market Price of Stock at Time of Repricing or Amendment (\$)	Exercise Price at Time of Repricing or Amendment (\$)	New Exercise Price (\$)	Length of Original Option Remaini Date Reprici Amend
Carl Spana	3/24/98	74,196	\$6.25	\$4.96	\$1.00	8 years 3
Charles Putnam (1)	3/24/98	74,196	\$6.25	\$4.96	\$1.00	8 years 3
Edward J. Quilty (2)	3/24/98	7,803	\$6.25	\$4.96	\$0.20	9 years 2
Edward J. Quilty	9/27/96	70,257	\$10.50	\$5.42	\$0.20	8 years 3

(1) Former executive vice president and chief operating officer.

(2) Former president and chief executive officer.

**EMPLOYMENT AGREEMENTS**

*Carl Spana, Ph.D. and Stephen T. Wills.* Dr. Spana and Mr. Wills each entered into an employment agreement with us for a two-year period commencing October 1, 2003. Dr. Spana is serving as chief executive officer and president at a salary of \$320,000 per year. Mr. Wills is serving as chief financial officer at a salary of \$265,000 per year. Each agreement also provides for:

annual bonus compensation, in an amount to be decided by the compensation committee and approved by the board, based on achievement of yearly objectives; and

participation in all benefit programs that we establish, to the extent the employee's position, tenure, salary, age, health and other qualifications make him eligible to participate.

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Each agreement allows us or the employee to terminate the agreement upon written notice, and contains other provisions for termination by the company for cause, or by the employee for good reason or due to a change in control (as these terms are defined in the employment agreements). Early termination may, in some circumstances, result in severance pay at the salary then in effect, for a period of 24 months (Spana) or 18 months (Wills), plus continuation of medical and dental benefits then in effect for 18 months. Termination following a change in control will result in a lump sum payment of two times (Spana) or one and one-half times (Wills) the salary then in effect, continuation of medical and dental benefits then in effect for 18 months, and immediate vesting of all stock options. Each agreement includes non-competition, non-solicitation and confidentiality covenants.

*Shubh D. Sharma, Ph.D.* Dr. Sharma entered into an employment agreement with us for a two-year period commencing October 1, 2003. Dr. Sharma is serving as a vice president and chief technical officer at a salary of \$185,000 per year. His agreement also provides for:

bonus compensation based on completion of proprietary peptide libraries, and discretionary incentive bonuses in an amount to be decided by the company; and

participation in all benefit programs that we establish, to the extent the employee's position, tenure, salary, age, health and other qualifications make him eligible to participate.

The agreement allows us or the employee to terminate the agreement upon written notice, and contains other provisions for termination by the company for cause (as defined in the agreement). Early termination may, in some circumstances, result in severance pay at the salary then in effect, for a period of six months. The agreement includes non-competition and confidentiality covenants.

*Perry B. Molinoff, M.D.* Dr. Molinoff entered into an employment agreement with us for a two-year period commencing September 4, 2001. His agreement automatically renewed for a one-year period unless terminated at least 30 days before the anniversary date. Dr. Molinoff served as executive vice president of research and development at a salary of \$265,000 per year. He resigned as an officer effective November 3, 2003, in order to accept appointment to the position of Vice Provost for Research at the University of Pennsylvania. He therefore no longer receives compensation or benefits under his employment agreement. His agreement also provided for:

annual bonus compensation, in an amount to be decided by the compensation committee and approved by the board, based on achievement of yearly objectives; and

participation in all benefit programs that we establish, to the extent the employee's position, tenure, salary, age, health and other qualifications make him eligible to participate.

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The agreement allowed us or the employee to terminate the agreement upon written notice, and contained other provisions for termination by the company for cause, or by the employee for good reason or due to a change in control (as these terms were defined in the employment agreement). Early termination could, in some circumstances, result in severance pay at the salary then in effect, plus continuation of medical and dental benefits then in effect, for a period

of 12 months. Termination following a change in control would have resulted in severance payments at the salary then in effect for 12 months, continuation of medical and dental benefits then in effect for 12 months, employment search expense reimbursement up to \$25,000, and immediate vesting of all stock options. Dr. Molinoff's resignation did not trigger the early termination provisions. The agreement included non-competition, non-solicitation and confidentiality covenants.

**COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION IN COMPENSATION DECISIONS.**

During the fiscal year ended June 30, 2003, Mr. deVeer, Dr. Horovitz and Kevin S. Flannery, a former director, served on the compensation committee. During the fiscal year ended June 30, 2004, Mr. deVeer, Dr. Horovitz, Dr. Taber and Dr. De Souza served on the compensation committee.

There are no compensation committee interlocks