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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2009

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission File Number: 000-51173

Targacept, Inc.
(Exact Name of Registrant as Specified in its Charter)

Delaware	**56-2020050**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
200 East First Street, Suite 300 Winston-Salem, North Carolina	**27101**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant's telephone number, including area code: (336) 480-2100

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of each class	Name of each exchange on which registered
Common Stock, $0.001 par value per share	**The NASDAQ Stock Market LLC (NASDAQ Global Market)**

Securities registered pursuant to Section 12(g) of the Exchange Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ☐ Yes ☒ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ☐ Yes ☒ No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ☐ Yes ☐ No

Indicate by check mark if disclosure of delinquent filers pursuant to Rule 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐	Accelerated filer ☐	Non-accelerated filer ☒ (Do not check if a smaller reporting company)	Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ☐ Yes ☒ No

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant as of June 30, 2009, was approximately $39,437,290, based on the price at which the registrant's common stock was last sold on June 30, 2009 ($2.45).

As of February 28, 2010, the registrant had 28,338,375 shares of common stock, $0.001 par value per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Specified portions of the registrant's proxy statement for its 2010 annual meeting of stockholders, which is expected to be filed pursuant to Regulation 14A within 120 days after the end of the registrant's fiscal year ended December 31, 2009, are incorporated by reference into Part III of this report.

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Cautionary Note Regarding Forward-Looking Statements

This annual report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, which we refer to as the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, which we refer to as the Exchange Act. For this purpose, any statements contained in this annual report, other than statements of historical fact, regarding: the progress, scope or duration of the development of TC-5214, AZD3480 (TC-1734), AZD1446 (TC-6683), TC-5619, TC-6987 or any of our other product candidates, such as the size, design, population, conduct or objective of any clinical trial, the timing for initiation or completion of or availability of results from any clinical trial or for submission or approval of any regulatory filing or for meeting with regulatory authorities, or any indication for which the product candidate may be developed; the benefits that may be derived from any of our product candidates; any payments that AstraZeneca or GlaxoSmithKline may make to us; the impact on our alliance of GlaxoSmithKline's shift in discovery research focus announced in February 2010; the period over which we will conduct grant-funded research and generate associated revenue; our operations, financial position, revenues, costs or expenses; or our strategies, prospects, plans, expectations or objectives are forward-looking statements made under the provisions of The Private Securities Litigation Reform Act of 1995. In some cases, words such as "may," "will," "could," "would," "should," "expect," "intend," "plan," "anticipate," "believe," "estimate," "predict," "project," "potential," "continue," "ongoing," "scheduled" or other comparable words identify forward-looking statements. Actual results, performance or experience may differ materially from those expressed or implied by forward-looking statements as a result of various important factors, including our critical accounting policies and the risks and uncertainties relating to: our dependence on the success of our collaborations with AstraZeneca and our alliance with GlaxoSmithKline; the significant control or influence that AstraZeneca has over the development of TC-5214, AZD3480 and AZD1446, including as to the scope, design and conduct of any future clinical trials; the conduct and results of clinical trials and non-clinical studies and assessments of TC-5214, AZD3480, AZD1446, TC-5619, TC-6987 or any of our other product candidates, including the performance of third parties engaged to execute them and difficulties or delays in subject enrollment and data analysis; our ability to establish additional strategic alliances, collaborations and licensing or other arrangements on favorable terms; and the timing and success of submission, acceptance and approval of regulatory filings. These and other risks and uncertainties are described in greater detail under the caption "Risk Factors" in Item 1A of Part I of this annual report and in other filings that we make with the Securities and Exchange Commission, or SEC. As a result of the risks and uncertainties, the results or events indicated by the forward-looking statements may not occur. We caution you not to place undue reliance on any forward-looking statement.

In addition, any forward-looking statement in this annual report represents our views only as of the date of this annual report and should not be relied upon as representing our views as of any subsequent date. We anticipate that subsequent events and developments may cause our views to change. Although we may elect to update these forward-looking statements publicly at some point in the future, we specifically disclaim any obligation to do so, except as required by applicable law. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make.

PART I

Item 1. Business.

Overview

We are a biopharmaceutical company engaged in the design, discovery and development of novel NNR Therapeutics™ for the treatment of diseases and disorders of the central nervous system. Our NNR Therapeutics selectively target neuronal nicotinic receptors, or NNRs. NNRs are found on nerve cells throughout the nervous system and serve as key regulators of nervous system activity.

We trace our scientific lineage to a research program initiated by R.J. Reynolds Tobacco Company in 1982 to study the activity and effects of nicotine, a compound that interacts non-selectively with all nicotinic receptors. Based on years of focused research in the NNR area, we believe that compounds that interact selectively with specific NNR subtypes have the potential to achieve positive medical effects by modulating their activity. We have built an extensive patent estate covering the structure or therapeutic use of small molecules designed to regulate the central nervous system by selectively affecting specific NNR subtypes.

We have multiple clinical-stage product candidates and preclinical programs in areas where we believe there are significant medical need and commercial potential, as well as proprietary drug discovery technologies. We also have two collaborations with AstraZeneca, one focused on TC-5214 as a treatment for major depressive disorder and one focused in cognitive disorders, as well as a strategic alliance with GlaxoSmithKline.

TC-5214

TC-5214 is a nicotinic channel blocker that is thought to derive antidepressant activity by modulating the activity of various NNR subtypes. In 2009, we completed a Phase 2b clinical trial of TC-5214 as an adjunct, or add-on, therapy in subjects with major depressive disorder who did not respond well to first-line treatment with a representative medicine from the drug class known as selective serotonin reuptake inhibitors. In the trial, the TC-5214 arm (TC-5214 plus citalopram hydrobromide) outperformed the add-on placebo arm (placebo plus citalopram hydrobromide) on the trial's primary outcome measure and all of the trial's secondary outcome measures, and the results were highly statistically significant. In December 2009, we entered into a collaboration and license agreement with AstraZeneca AB for the global development and commercialization of TC-5214. In this annual report, we refer to the agreement as our 2009 agreement with AstraZeneca.

AZD3480 (TC-1734) and AZD1446 (TC-6683)

AZD3480 (TC-1734) and AZD1446 (TC-6683) are both novel small molecules that modulate the activity of the a4ß2 NNR. We have a collaborative research and license agreement with AstraZeneca AB that we entered into in December 2005 for the development and worldwide commercialization of AZD3480 and AZD1446 as treatments for various conditions characterized by cognitive impairment. In this annual report, we refer to the agreement as our 2005 agreement with AstraZeneca.

In 2009, we and AstraZeneca completed a Phase 2 clinical trial of AZD3480 in adults with ADHD in which AZD3480 met the primary outcome measure. Previously, we or AstraZeneca had completed clinical trials of AZD3480 in various indications characterized by cognitive impairment that generated a range of efficacy results, including: (1) achievement of primary outcome measures (our Phase 2 trial in age associated memory impairment, or AAMI, a common condition characterized by gradual memory loss or other cognitive impairment that generally occurs with normal aging, reported in 2006); (2) inconclusive (AstraZeneca's Phase 2b trial in mild to moderate Alzheimer's disease completed in 2008); and (3) failure to achieve primary outcome measures (AstraZeneca's Phase 2b trial in cognitive dysfunction in schizophrenia completed in 2008). We expect AstraZeneca to conduct future clinical development of AZD3480 in ADHD. Whether additional development of AZD3480 will be conducted in the future in Alzheimer's disease or any other indication is uncertain.

We discovered and advanced AZD1446 as part of a multi-year research collaboration conducted under our 2005 agreement with AstraZeneca. AstraZeneca completed multiple Phase 1 clinical trials of AZD1446 in 2009 and has a number of additional clinical trials ongoing, including a clinical trial designed to assess safety and tolerability in subjects with Alzheimer's disease and a Phase 2 clinical trial in adults with ADHD. We expect AstraZeneca to conduct further development of AZD1446 in either or both of Alzheimer's disease and ADHD.

TC-5619

TC-5619 is a novel small molecule that modulates the activity of the a7 NNR. We initiated a Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia in the fourth quarter of 2009 pursuant to a development plan that we agreed upon with AstraZeneca. As a result of a process that we initiated in 2007 under our 2005 agreement with AstraZeneca and a related election made by AstraZeneca, we agreed to develop TC-5619 independently through Phase 1 clinical development and a Phase 2 clinical proof of concept trial pursuant to an agreed development plan. Following our completion of the development plan, AstraZeneca has the right to license TC-5619 and to further develop and potentially commercialize TC-5619 for various conditions characterized by cognitive impairment on terms specified in the 2005 agreement.

TC-6987

TC-6987 is a novel small molecule that modulates the activity of the a7 NNR. We are conducting Phase 1 clinical development of TC-6987. We are considering multiple indications for a potential Phase 2 clinical trial of TC-6987 if our Phase 1 development is successful, including various disorders characterized by inflammation.

GlaxoSmithKline Alliance

We have a product development and commercialization agreement with SmithKline Beecham Corporation, doing business as GlaxoSmithKline, and Glaxo Group Limited, that we entered into in July 2007. In this annual report, we refer to SmithKlineBeecham Corporation and Glaxo Group Limited collectively as GlaxoSmithKline.

Our agreement with GlaxoSmithKline sets forth the terms of an alliance designed to discover, develop and market product candidates that selectively target specified NNR subtypes in five therapeutic focus areas—pain, smoking cessation, addiction, obesity and Parkinson's disease. In February 2010, GlaxoSmithKline announced plans to cease discovery research in selected neuroscience areas, specifically including pain. Discussions with GlaxoSmithKline regarding the effects of its strategic change on our alliance are ongoing. Until these discussions are completed, the overall impact is uncertain, but we currently anticipate that multiple therapeutic focus areas in the alliance will be discontinued.

Under the agreement, we have agreed, for specified periods of time and at our sole expense, to use diligent efforts to conduct research activities designed to discover product candidates that target specified NNR subtypes, to develop the product candidate identified as the lead for each therapeutic focus area through a Phase 2 clinical proof of concept trial and to develop up to two other product candidates for each therapeutic focus area to a specified stage of preclinical development. With respect to each therapeutic focus area in the alliance, if we achieve clinical proof of concept with a lead product candidate, GlaxoSmithKline would have an exclusive option for an exclusive license to that lead product candidate and up to two other product candidates in development in the alliance for the same therapeutic focus area on a worldwide basis. If GlaxoSmithKline exercises its option and pays a non-refundable exercise fee, GlaxoSmithKline would become responsible for using diligent efforts to conduct later-stage development and commercialization of the lead product candidate at its sole expense. GlaxoSmithKline's exclusive license would include all fields of use other than those indications for which AstraZeneca has development and commercialization rights under our 2005 agreement with AstraZeneca.

Pentad™

Our drug discovery activities utilize sophisticated proprietary computer-based molecular design methodologies and extensive biological and chemical data for a library of diverse compounds developed and collected over more than 20 years. We refer to these technologies collectively as Pentad.

Role of NNRs in the Nervous System

The human nervous system is a massive communications network that sends and receives information throughout the body via billions of specialized nerve cells known as neurons. Neurons continually gather information about the body's internal and external environment and send signals to the brain. These signals pass from one neuron to another across a gap between a communicating neuron and a receiving neuron known as a synapse. Electrical impulses of a communicating neuron are converted into chemicals called neurotransmitters that are released by the communicating neuron and bind to specialized proteins known as receptors located across the synapse on the receiving neuron to enable the signal to continue. The major neurotransmitters in the brain include dopamine, serotonin, norepinephrine, glutamate, gamma-aminobutyric acid, or GABA, and acetylcholine.

NNRs are a class of receptors found in the nervous system that play a critical role in modulating the release of neurotransmitters to regulate nervous system activity. When the neurotransmitter acetylcholine is released from a nearby neuron, called an interneuron, and binds to an NNR on a communicating neuron, the flow of neurotransmitters from the communicating neuron to a receiving neuron is adjusted by the NNR. This action, known as neuromodulation, results in a greater release of neurotransmitters across the synapse when the nervous system is understimulated and a lesser release of neurotransmitters across the synapse when the nervous system is overstimulated. As neuromodulators, NNRs serve as the nervous system's self-adjusting "volume knob."

The nervous system will not operate properly if the relative levels of key neurotransmitters in the brain are not maintained in a normal balance. A disruption in this balance can cause many common nervous system diseases and disorders. We believe that compounds that target NNRs to modulate their activity have the potential to restore this balance and therefore promise as treatments for these diseases and disorders.

NNRs are comprised of five protein subunits that are arranged like staves of a barrel around a central pore. Each combination of five subunits represents an NNR subtype. There are several subtypes, each of which is identified by Greek letters. Scientific evidence has established that individual NNR subtypes have particular functions in the body that are relevant to a number of debilitating diseases and disorders.

Many published studies describing beneficial effects of nicotine in humans and animals and the higher prevalence of diseases such as Alzheimer's disease and Parkinson's disease in non-smokers as compared to smokers, as well as the entry to the market of Pfizer's smoking cessation product Chantix (which acts on several NNR subtypes as well as other molecular targets in the body and is known outside of the United States as Champix), suggest the therapeutic potential of compounds that interact with NNRs. However, despite their beneficial effects, these compounds have historically not been desirable as therapies because they have not been sufficiently selective. This means that these compounds interact not only with NNRs, but also with nicotinic receptors in the muscles and in groups of nerve cells known as ganglia that are associated with adverse effects such as increased heart rate, high blood pressure, irregular heartbeat, nausea, vomiting and a dangerous slowing of breathing known as respiratory depression. Based on years of focused research in the NNR area, we are developing product candidates that are designed to interact selectively with specific NNR subtypes to promote positive medical effects and limit adverse side effects.

Our Business Strategy

Our mission is to provide superior treatment options for complex diseases and disorders and improve patient lives by developing innovative new medicines that exploit the unique role of NNRs. To achieve our mission, our goal is to leverage our experience and expertise in the biology of NNRs and the discovery and development of

novel drugs that selectively target them to become a leader in the commercialization of NNR Therapeutics for diseases and disorders where there is significant medical need and commercial potential. To achieve this goal, we are pursuing the following strategies:

- We believe that drugs designed to selectively target specific NNR subtypes can have positive medical effects with limited adverse side effects. We intend to continue to use our scientific expertise and Pentad to discover compounds that selectively target specific NNR subtypes as potential treatments for diseases and disorders of the central nervous system.
- We have two collaborations with AstraZeneca, one focused on TC-5214 as a treatment for major depressive disorder and one focused in cognitive disorders. We also have a strategic alliance with GlaxoSmithKline. We intend to selectively seek additional alliances and collaborations to assist us in furthering the development of some of our product candidates. In particular, we intend to enter into these alliances and collaborations for target indications for which our potential collaborator has particular expertise or that involve large primary care markets that must be served by large sales and marketing organizations. In entering into these alliances and collaborations, our goal will generally be to maintain co-promotion or co-commercialization rights for specialists, particularly in neurology and psychiatry, in the United States and, potentially in some cases, other markets. Under our agreements with AstraZeneca, we have the option to co-promote TC-5214 and AZD3480, as well as AZD1446 and any other licensed compounds that arose out of the research collaboration, to specified classes of physicians in the United States.
- We have established ourselves as a leader in NNR research over more than 20 years. Our leadership position in this area is reflected in the numerous NNR-related articles and abstracts published by our scientists in prominent scientific journals, as well as our extensive patent estate. We intend to continue to invest significant resources to remain at the forefront of NNR research, build upon our NNR expertise and expand our intellectual property portfolio. We also plan to augment our own research by collaborating with commercial and academic institutions that seek access to our proprietary knowledge and compounds.
- We have identified numerous indications in which NNRs have been implicated and for which we believe that drugs that selectively target specific NNR subtypes can potentially provide a medical benefit. We prioritize our product development opportunities in an effort to apply our product pipeline to indications in which there is a significant medical need and commercial potential.

Our Product Development Pipeline

The following table summarizes our pipeline of clinical-stage product candidates.

Product Candidate	Planned Target Indication(s)	Status of Development	Commercial Rights
TC-5214	Major depressive disorder (adjunct therapy, second-line "switch" monotherapy)	Phase 2b clinical trial completed; initiation of Phase 3 development expected mid 2010	AstraZeneca
AZD3480 (TC-1734)	ADHD	Phase 2 clinical trial in adults with ADHD completed; initiation of Phase 2b clinical trial in adults with ADHD expected in the second half of 2010	AstraZeneca
AZD1446 (TC-6683)	Either or both of Alzheimer's disease and ADHD	Multiple Phase 1 trials completed; a number of additional trials ongoing, including as an add-on treatment to donepezil in subjects with Alzheimer's disease and a Phase 2 clinical trial in adults with ADHD	AstraZeneca
TC-5619	Cognitive dysfunction in schizophrenia and potentially one or more other conditions characterized by cognitive impairment	Phase 2 clinical trial in cognitive dysfunction in schizophrenia ongoing	subject to option of AstraZeneca*
TC-6987	One or more disorders characterized by inflammation	Phase 1 trial ongoing	Targacept, but potentially subject to option of GlaxoSmithKline**

* Following completion of an agreed development plan through a Phase 2 clinical proof of concept trial, AstraZeneca has the right to license TC-5619 for various conditions characterized by cognitive impairment and on terms specified in our 2005 agreement with AstraZeneca.

** If TC-6987 is developed for a therapeutic focus area of the alliance and achieves Phase 2 clinical proof of concept, GlaxoSmithKline would have an exclusive option for an exclusive license on a worldwide basis for all fields of use other than those indications for which AstraZeneca has development and commercialization rights under our 2005 agreement with AstraZeneca.

Information regarding our research and development expenses for the fiscal years ended December 31, 2009, 2008 and 2007 is included under "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this annual report. All of our long-lived assets are located in the United States.

TC-5214

TC-5214 is a nicotinic channel blocker that is thought to derive antidepressant activity by modulating the activity of various NNR subtypes and is in development as a treatment for major depressive disorder. TC-5214 is one of the two enantiomers of the racemate mecamylamine hydrochloride. Enantiomers are mirror images of each other that have the same chemical but potentially different biological properties and together form a chemical mixture known as a racemate.

We are co-developing TC-5214 with AstraZeneca under our 2009 agreement with AstraZeneca. The initial global clinical program is planned to include development of TC-5214 as an adjunct therapy and as a second-line "switch" monotherapy, in each case in adults with major depressive disorder who do not respond adequately to first-line antidepressant treatment. AstraZeneca is responsible for 80% of the costs of the initial program, except that AstraZeneca is responsible for 100% of development costs that are required only to obtain or maintain regulatory approval in countries outside the United States and the European Union. We are responsible for 20% of the costs of the initial program but have the right to terminate our obligation to fund our share of these costs once we have funded a specified amount. If we fund the specified amount and terminate our obligation to fund our share of further costs of the initial development program, any future milestones and royalties payable to us under the agreement would be reduced by the amount of our unfunded share plus interest, subject to a maximum reduction that may be applied to any one payment.

Completed Phase 2b Clinical Trial in Major Depressive Disorder. In 2009, we completed a Phase 2b clinical trial of TC-5214 as an adjunct, or add-on, therapy in subjects with major depressive disorder who did not respond well to first-line treatment with citalopram hydrobromide. Citalopram, an approved treatment for major depressive disorder marketed in the United States as Celexa, is a representative medicine from the drug class known as selective serotonin reuptake inhibitors, or SSRIs, which is the drug class most commonly prescribed for major depressive disorder.

The Phase 2b clinical trial was a two-phase study conducted at 20 sites in India and three sites in the United States. The first phase of the trial was "open label," which means both the subjects and the investigators knew what was being administered. In the first phase, 579 subjects received first-line treatment with citalopram hydrobromide for eight weeks, 20mg daily for the first four weeks and 40mg daily for the next four weeks. At the end of the eight weeks, subjects whose score on the Montgomery-Asberg Depression Rating Scale, or MADRS, which is a scale on which the clinician evaluates the subject's depressed mood and other symptoms of depression and anxiety, had improved less than 50 percent and was no lower than 17 and whose score on the Clinical Global Impression—Severity of Illness subscale, or CGI-S, which is a scale on which the clinician assesses how ill a subject is based on his or her total clinical experience, was no lower than 4 were considered partial or non responders and randomized into the second phase of the trial.

The second phase of the trial was double blind and placebo controlled. The term "double blind" means that neither the subjects nor the investigators knew which subjects were receiving TC-5214 and which subjects were receiving placebo. In the second phase, subjects continued their citalopram treatment and also received either add-on TC-5214 or add-on placebo for an additional eight weeks. The daily dosage of TC-5214 was initially 2mg and could be increased at the discretion of the investigator to 4mg and to 8mg based on tolerability and therapeutic response.

The primary outcome measure for the trial was mean change between add-on TC-5214 (TC-5214 + citalopram) and add-on placebo (placebo + citalopram) from double blind baseline as measured by the Hamilton Rating Scale for Depression-17, or HAM-D, which is another scale on which the clinician evaluates the subject's depressed mood and other symptoms of depression and anxiety, at week 16. The magnitude of clinical response on HAM-D was 6.0 points greater for the add-on TC-5214 arm (13.75 point improvement) than for the add-on placebo arm (7.75 point improvement), and the result was highly statistically significant in favor of TC-5214 ($p < 0.0001$) on an intent to treat basis. The results on all of the trial's secondary efficacy outcome measures, including MADRS, the Quick Inventory of Depressive Symptomatology—Self Reporting scale and

assessments of irritability, disability, cognition, severity of illness and global improvement, were also highly statistically significant in favor of TC-5214 ($p < 0.0001$) on an intent to treat basis. The intent to treat dataset included 265 subjects in the second phase.

TC-5214 exhibited a favorable tolerability profile in the trial. The most frequent adverse events were headache, dizziness and constipation, and there was no clinically significant difference between the dose groups in discontinuations due to adverse events. There was one serious adverse event in the trial considered by the investigators to be related to study drug (either or both of citalopram and TC-5214), a seizure experienced by a study subject.

Major depressive disorder is characterized by a combination of symptoms that interfere with a person's ability to work, sleep, study, eat and enjoy once-pleasurable activities. It is disabling and can prevent a person from functioning normally. A 2009 report from the market research firm Decision Resources estimated that approximately 42.2 million people suffer from major depressive disorder in the world's seven major pharmaceutical markets—the United States, France, Germany, Italy, Spain, the United Kingdom and Japan. The Sequenced Treatment Alternatives to Relieve Depression, or STAR*D, study undertaken by the National Institute of Mental Health between 2001 and 2006 showed the inadequacy of currently available therapies for major depressive disorder. In the first phase of the STAR*D study, approximately 2,800 persons with major depressive disorder were given the representative SSRI citalopram for 12 to 14 weeks. Only about one-third of the participants became symptom free, which is referred to as achieving "remission," and about 10-15 percent more responded, but did not reach remission.

AZD3480 (TC-1734)

AZD3480 (TC-1734) is a novel small molecule that modulates the activity of the a4ß2 NNR and is in development under our 2005 agreement with AstraZeneca. We or AstraZeneca have completed Phase 2 clinical trials of AZD3480 in various indications characterized by cognitive impairment, including adults with ADHD, Alzheimer's disease, cognitive dysfunction in schizophrenia, AAMI and mild cognitive impairment, or MCI. AstraZeneca is responsible for conducting and funding future clinical development and potential future commercialization of AZD3480. We expect AstraZeneca to conduct future clinical development of AZD3480 in ADHD. Whether additional development of AZD3480 will be conducted in the future in Alzheimer's disease or any other indication is uncertain.

Completed Phase 2 Trial in Adults with ADHD

In 2009, we and AstraZeneca completed a Phase 2 clinical trial of AZD3480 in adults with ADHD. The trial was a double blind, placebo controlled crossover study conducted at Fletcher Allen Health Care, an affiliate of University of Vermont College of Medicine. Subjects were non-smoking males and females between the ages of 18 and 65 who were diagnosed with ADHD based on DSM-IV criteria and had a baseline score of at least 4 on CGI-S. Each subject received 5mg AZD3480, 50mg AZD3480 and placebo daily for two weeks, in random order, with the three dosing periods separated by three-week periods without any dosing to minimize carryover effects. As a result, each subject served as his or her own control.

The primary outcome measure for the trial was the change in total symptom score on the Conners Adult ADHD Rating Scale—Investigator Rating, or CAARS-INV, a scale that takes into account nine domains thought to encompass a range of ADHD manifestations in adults, following two weeks dosing with AZD3480 as compared to two weeks dosing with placebo. In the trial, the subjects' symptoms of ADHD as measured by CAARS-INV improved with 50mg AZD3480, and the result was statistically significant ($p < 0.01$) on an intent to treat basis. Data from the study on CAARS-INV are shown in the table below.

	CAARS-INV			
	Completed Subjects	Pre-Treatment Mean (Standard Deviation)	Post-Treatment Mean (Standard Deviation)	Mean Change (Standard Deviation)
Placebo	24	37.7(5.45)	36.9(5.20)	0.8(5.33)
5mg AZD3480	23	39.6(5.36)	34.9(5.24)	4.7(5.30)
50mg AZD3480	24	40.3(5.40)	33.1(5.34)	7.2(5.37)

Statistically significant results were also achieved at 50mg AZD3480 on some of the secondary outcome measures in the study, including Stop Signal Reaction Time, a computerized assessment of behavioral inhibition, which is a core cognitive deficit of ADHD. AZD3480 was well tolerated in the study, and there were no serious adverse events.

ADHD is a condition that develops during childhood and, if not adequately treated, can have long-term adverse effects into adolescence and adulthood. The principal characteristics of ADHD are inattention, hyperactivity and impulsivity. For an adult to be diagnosed with ADHD, the ADHD symptoms must have begun during childhood and continued throughout adulthood. The market research firm Business Insights has estimated that, in 2008, there were approximately 25 million adults and 12.7 million children with ADHD in the world's seven major pharmaceutical markets. The most commonly used treatments for ADHD are from the drug class known as stimulants. Because stimulants have potential for abuse, they are scheduled and and can therefore be burdensome for patients. All of the currently available treatments for ADHD have side effects, such as increased heart rate and blood pressure, loss of appetite, insomnia and behavioral changes like irritability.

Completed Phase 2b Clinical Trial in Mild to Moderate Alzheimer's Disease

In 2008, AstraZeneca completed two Phase 2b double blind, placebo controlled, dose finding clinical trials of AZD3480, one in mild to moderate Alzheimer's disease and one in cognitive dysfunction in schizophrenia. The trial in mild to moderate Alzheimer's disease, known as the "Sirocco" trial, was conducted at 84 sites in Western Europe, Eastern Europe and Canada. In the Sirocco trial, 567 subjects who were between 60 and 85 years old and diagnosed with probable Alzheimer's disease classified as mild or moderate in severity were randomly assigned to one of three dose groups of AZD3480, to the active comparator donepezil, or to placebo and dosed over a 12-week period. The primary outcome measure of the trial was change from baseline after 12 weeks on the Alzheimer's Disease Assessment Scale-cognitive subscale, or ADAS-Cog. Some of the secondary outcome measures of the trial included the Alzheimer's Disease Cooperative Study—Clinical Global Impression of Change, or ADCS-CGIC, which is a 7-point clinician assessment of change in behavior and the ability to function, the Mini Mental State Examination, or MMSE, which is a quantitative, 30-point cognition scale, and a computer-based test battery developed by CDR Ltd. to test cognitive function.

The results of the Sirocco trial were inconclusive. Neither the active comparator donepezil nor AZD3480 met the trial's criteria for statistical significance on the primary outcome measure, ADAS-Cog. On the secondary outcome measures, subjects dosed with AZD3480 showed an improvement on ADCS-CGIC and the MMSE at two of the three doses tested as compared to subjects dosed with placebo. Of the three AZD3480 doses evaluated, subjects in the middle dose group showed the most improvement on both measures as compared to subjects dosed with placebo, with a 0.5 point advantage on ADCS-CGIC and a 0.9 point advantage on the MMSE. Subjects dosed with donepezil also showed an improvement as compared to subjects dosed with placebo on ADCS-CGIC, with a 0.2 point advantage, and the MMSE, with a 1.0 point advantage. No improvement was shown in any domain of the CDR test battery in the pooled dataset of all subjects in the donepezil dose group or any of the AZD3480 dose groups as compared to the placebo dose group. AZD3480 exhibited an overall safety and tolerability profile comparable to placebo in the trial.

Alzheimer's disease, the most common form of dementia, is a debilitating brain disorder for which there is no cure. Decision Resources has estimated that, in 2008, there were approximately 6.3 million people with Alzheimer's disease in the world's seven major pharmaceutical markets. The disease progresses in stages from mild to moderate to severe and gradually destroys a person's memory and ability to learn, reason, make judgments, communicate and carry out daily activities. Mild Alzheimer's disease is characterized by mild forgetfulness and difficulty acquiring basic information and communicating. Patients generally exhibit the symptoms of mild Alzheimer's disease for two to four years before progressing to the moderate stage. Moderate Alzheimer's disease is characterized by forgetfulness, failure to recognize friends and family, disorientation regarding time and place and personality changes. Patients generally exhibit the symptoms of moderate Alzheimer's disease for up to ten years before progressing to the severe stage. Severe Alzheimer's disease is

characterized by difficulty performing simple tasks and activities associated with daily living. Patients with severe Alzheimer's disease require continuous care and generally do not survive for more than three years.

Completed Phase 2b Clinical Trial in Cognitive Dysfunction in Schizophrenia

AstraZeneca's Phase 2b clinical trial of AZD3480 in cognitive dysfunction in schizophrenia completed in 2008, known as the "HALO" trial, was conducted at approximately 70 enrolling sites in the United States and Canada. In the trial, 445 subjects diagnosed with schizophrenia who were between 18 and 55 years old, active smokers, taking a marketed drug from the class known as atypical anti-psychotics and clinically stable were randomly assigned to one of three dose groups of AZD3480 or to placebo and dosed, together with continued treatment with the applicable atypical anti-psychotic, over a 12-week period. The primary endpoints of the trial were change from baseline after 12 weeks on scores for attention/vigilance, working memory, verbal learning, speed of processing and reasoning and problem solving as measured by a computerized test battery known as IntegNeuro. As used in this annual report, the terms "endpoint" and "outcome measure" have the same meaning. AZD3480 did not meet the HALO trial's criteria for statistical significance on any of the primary endpoints.

Completed Phase 2 Clinical Trial in AAMI Reported in 2006

In 2006, we reported results from a double blind, placebo controlled Phase 2 clinical trial of AZD3480 in AAMI in the United States. We recruited 193 subjects between the ages of 50 and 80, who were classified with AAMI based on inclusion criteria reflecting both subjective and objective memory impairment, to participate in the trial. The trial assessed the effects of 25mg AZD3480 and 50mg AZD3480 on various aspects of cognitive function using the CDR test battery. We tested each subject at various time points prior to the first day of the 16-week dosing period to establish baseline. We tested subjects again at eight weeks and on the last day of the 16-week dosing period. The CDR test battery includes measures of attention, speed of cognitive processes and memory that assess the ability to react to stimuli, recognize words and pictures and recall words. These measures are then used to make composite assessments on five factors —power of attention, continuity of attention, working or short-term memory, episodic or long-term memory and speed of memory.

There were three co-primary efficacy endpoints for the trial, including:

- *power of attention*—change from baseline on the power of attention factor of the CDR test battery at the end of the 16-week dosing period, as compared to placebo;
- *episodic memory*—change from baseline on the episodic memory factor of the CDR test battery at the end of the 16-week dosing period, as compared to placebo; and
- *subject global impression*—composite score on a cognitive performance scale comprised of three seven-point measures in which each subject rates himself or herself on attention, memory and speed of thinking at the end of the 16-week dosing period, as compared to placebo.

On an intent to treat basis, subjects in the 50mg AZD3480 dose group showed improvement as compared to subjects in the placebo dose group on all three co-primary efficacy endpoints and subjects in the 25mg AZD3480 dose group showed improvement as compared to subjects in the placebo dose group on the power of attention endpoint. These results were statistically significant, with p-values less than 0.05.

Previously Completed Phase 2 Clinical Trials in AAMI and MCI

Prior to the Phase 2 clinical trial of AZD3480 in AAMI described above, we completed two double blind, placebo controlled, crossover design Phase 2 clinical trials of AZD3480, one in AAMI and one in MCI. In the AAMI trial, we evaluated four doses of AZD3480, 50mg, 100mg, 125mg and 150mg. In the MCI trial, we evaluated two doses of AZD3480, 50mg and 100mg. Each trial assessed the effects of AZD3480 on various aspects of cognitive function using the CDR test battery before dosing and at various time points after dosing on the first and last day of each dosing period.

In both trials, AZD3480 demonstrated positive effects at some dose levels with respect to some measures of cognition tested, but did not demonstrate positive effects as to all measures at all dose levels and placebo showed superior effects to AZD3480 as to some measures at some dose levels. The results of the AAMI trial were most favorable in the 50mg AZD3480 dose group and were less pronounced in the other dose groups. The results of the MCI trial were more favorable in the 100mg AZD3480 dose group, as the results in the 50mg AZD3480 dose group did not favor AZD3480 on any measure.

AZD1446 (TC-6683)

AZD1446 (TC-6683) is a novel small molecule that modulates the activity of the a4ß2 NNR and, like AZD3480, is in development under our 2005 agreement with AstraZeneca.

We discovered and advanced AZD1446 as part of a multi-year research collaboration that we and AstraZeneca conducted under our 2005 agreement with AstraZeneca. The research collaboration expired in January 2010. AstraZeneca is responsible for conducting and funding the development and potential future commercialization of AZD1446. AstraZeneca completed multiple Phase 1 clinical trials of AZD1446 in 2009 and has a number of additional clinical trials ongoing, including a clinical trial designed to assess safety and tolerability in subjects with Alzheimer's disease and a Phase 2 clinical trial in adults with ADHD. AZD1446 is planned for further development in either or both of Alzheimer's disease and ADHD.

TC-5619

TC-5619 is a novel small molecule that modulates the activity of the a7 NNR. We initiated a Phase 2 clinical trial of TC-5619 as a treatment for cognitive dysfunction in schizophrenia in the fourth quarter of 2009 pursuant to a development plan that we agreed upon with AstraZeneca.

We have previously completed a Phase 1 single rising dose clinical trial and a Phase 1 multiple rising dose clinical trial of TC-5619. In a single rising dose trial, each subject in a dose group receives a single dose of the agent being evaluated, with subjects in each subsequent dose group receiving a pre-determined higher dosage than subjects in the preceding dose group. In a multiple rising dose trial, each subject in a dose group receives multiple doses of the agent being evaluated, with subjects in each subsequent dose group receiving a pre-determined higher dosage than subjects in the preceding dose group. TC-5619 was generally well tolerated in both Phase 1 trials at doses that would provide a substantial therapeutic margin based on the doses being evaluated in our ongoing Phase 2 clinical trial. In addition, in our Phase 1 multiple rising dose trial, we used the five factors from the CDR test battery as surrogate efficacy measures and observed a signal in favor of TC-5619 on the power of attention factor.

In a 2004 survey of 46 cognitive neuroscientists and neuropharmacologists conducted in connection with a National Institute of Mental Health initiative known as Measurement and Treatment Research to Improve Cognition in Schizophrenia, or MATRICS, a7 was selected more often than any other target as the target of most interest in the development of treatments for cognitive dysfunction in schizophrenia.

We plan to conduct our Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia at sites in India and the United States, but the study is currently ongoing only at U.S. sites. The trial is designed as a double blind, placebo controlled, randomized, parallel group study. The trial is planned to include up to 200 subjects who are taking an approved medication from the drug class known as atypical anti-psychotics, approximately 50% of whom are tobacco users and approximately 50% of whom are not tobacco users. The trial design provides for subjects to be randomly assigned to one of three dose groups of TC-5619 or to placebo and dosed over a 12-week period. The primary outcome measure of the trial is change from baseline on the Groton Maze Learning item of the CogState Schizophrenia Test Battery, a computerized battery of neuropsychiatric tests that assess specific cognitive domains, on each of three measurement dates as compared to placebo.

In 2007, we initiated a process under our 2005 agreement with AstraZeneca pursuant to which we offered AstraZeneca the right to license TC-5619 for specified conditions characterized by cognitive impairment. As permitted by the 2005 agreement, AstraZeneca made an election in November 2007 pursuant to which we would develop TC-5619 independently through Phase 1 clinical development and a Phase 2 clinical proof of concept trial in accordance with an agreed development plan, following which AstraZeneca would have the right to license TC-5619 for various conditions characterized by cognitive impairment on terms specified in the 2005 agreement. As a result, AstraZeneca made a $2 million payment to us in the fourth quarter of 2007. If TC-5619 achieves clinical proof of concept and AstraZeneca exercises its right to license TC-5619, the 2005 agreement provides for AstraZeneca to make a $40 million payment to us and to assume responsibility for and fund all future development and commercialization. In that event, we would be eligible to receive additional payments of up to $226 million, contingent upon the achievement of development, regulatory, first commercial sale and first detail milestones for three indications, as well as stepped double-digit royalties on any future product sales. If TC-5619 does not achieve clinical proof of concept but AstraZeneca remains interested in a potential license, the 2005 agreement provides for us and AstraZeneca to negotiate terms. Under the 2005 agreement, we would not have been permitted to develop TC-5619 for specified conditions characterized by cognitive impairment without first offering AstraZeneca the right to license TC-5619.

Schizophrenia is a chronic, severe and disabling form of psychosis. In addition to symptoms such as delusions, hallucinations, the inability to disregard familiar stimuli, sometimes referred to as sensory gating, disorganized speech, grossly disorganized or catatonic behavior and prolonged loss of emotion, feeling, volition or drive, schizophrenia is often marked by impairment in cognitive functions, such as attention, vigilance, memory, and reasoning. Business Insights has estimated that, in 2007, there were approximately 7.9 million people with schizophrenia in the world’s seven major pharmaceutical markets. It has been estimated that up to 75% of persons with schizophrenia are cognitively impaired. There is currently no drug approved in the United States or Europe specifically for cognitive dysfunction in schizophrenia.

TC-6987

TC-6987 is a novel small molecule that modulates the activity of the a7 NNR. We are conducting Phase 1 clinical development of TC-6987. We are considering multiple indications for a potential Phase 2 clinical trial of TC-6987 if our Phase 1 development is successful, including various disorders characterized by inflammation.

TC-6499

TC-6499 is a novel small molecule that modulates the activity of the a4ß2 NNR. We previously evaluated TC-6499 as a pain treatment. In March 2009, we announced that the results from a Phase 1 multiple rising dose trial did not project a therapeutic margin sufficient to support further development of TC-6499 as a treatment for neuropathic pain. Based on the activity of TC-6499 at certain NNR subtypes located in the gastrointestinal tract, we believe it may have potential as a treatment for certain gastrointestinal disorders and are considering conducting an exploratory study in irritable bowel syndrome.

TC-5685

TC-5685 is a preclinical product candidate that inhibits the activity of the a4ß2 NNR and is an enantiomer of our compound TC-2216. We previously completed a Phase 1 single rising dose clinical trial of TC-2216 in healthy volunteers. We do not plan to conduct further clinical development of TC-2216 and anticipate that we will instead focus development resources that might otherwise be allocated to TC-2216 to progress TC-5685.

Our Preclinical Research Programs

In addition to our clinical-stage product candidates, we focus preclinical research efforts in areas in which we believe NNRs can be exploited for medical benefit and for which we believe we can efficiently develop marketable product candidates. We have preclinical research programs in smoking cessation, addiction, obesity,

pain and Parkinson's disease, which currently are the therapeutic focus areas of our agreement with GlaxoSmithKline. In addition, we have a program focused on the role of NNRs in inflammation involving the affecting of cytokines. The financial resources that we apply to and the progress that we may make in any particular preclinical program may vary from period to period and year to year.

Smoking Cessation

Due primarily to nicotine's addictive effects, it is very difficult to quit smoking. Published studies have linked nicotine's addictive effects to the release of dopamine in regions in the brain involved in feelings of reward and pleasure. Although the specific NNRs implicated in the regulation of dopamine are not fully characterized, several reported studies suggest that the a6, a4, ß2 and ß4 NNR subunits may be involved. These studies have shown that selectively modulating NNRs that include a6, a4, ß2 or ß4 subunits reduced the rewarding effects of nicotine administration in mice or the withdrawal effects of stopping nicotine administration in mice. Other studies have shown that mice deficient in the ß2 NNR subunit failed to self-administer nicotine and had reduced activity in the brain regions associated with reward and pleasure.

In addition, we are a named subcontractor on a grant awarded by the National Institute on Drug Abuse, part of the National Institutes of Health, to The California Institute of Technology to fund research on innovative NNR-based approaches to the development of therapies for smoking cessation. In addition to The California Institute of Technology, we are collaborating with University of Colorado at Boulder to conduct this research.

Addiction

There is also a need for more effective treatments to help addicts reduce or eliminate their intake of other drugs of abuse besides nicotine. Although other drugs of abuse may activate different targets in the brain than nicotine, they act generally by increasing levels of dopamine. The dopamine system is thought to be the common pathway by which these drugs produce feelings of pleasure and reward. As described above, an association has been shown between certain NNR subunits and brain activity associated with reward and pleasure. Accordingly, we believe that compounds that modulate NNRs may have the potential to decrease the rewarding effects of drugs of abuse such as alcohol or cocaine.

Obesity

A number of published studies have demonstrated that smokers generally weigh significantly less than non-smokers, and nicotine is believed to be responsible. These studies have also shown that smokers often gain weight when they stop smoking. Moreover, reported studies with animals have shown that food intake and body weight gain are reduced following repeated administration of nicotine and that the effects are reversed when nicotine administration is stopped. A number of NNRs are thought to play a role in appetite and metabolism.

Pain

Pain is a common endpoint for many different conditions, injuries and disease states. Pain can be short-term or persistent and nociceptive or neuropathic in nature. Multiple NNR subunits are found in pain pathways. Scientific evidence suggests that multiple NNRs may have potential therapeutic application for a broad range of pain states.

Parkinson's disease

Parkinson's disease is a movement disorder associated with a deficit in dopamine in the brain resulting from a progressive deterioration and death of cells in the brain, which is known as neurodegeneration. As noted above, several reported studies suggest that the a6, a4 and ß2 NNR subunits may be involved in regulating dopamine release. As a result, NNRs that contain one or more of these subunits may have promise as therapeutic targets for

the treatment of Parkinson's disease. Moreover, the existence of many published studies showing the greater prevalence of Parkinson's disease in non-smokers as compared to smokers further suggests the potential application of compounds that interact with NNRs as treatments for Parkinson's disease.

We have been awarded two grants from The Michael J. Fox Foundation for Parkinson's Research, one to fund research to test the potential of compounds that modulate NNRs to address Levodopa-induced abnormal involuntary movements, known as dyskinesias, and the other to fund research to identify NNR-related biomarkers relevant to Parkinson's disease. Levodopa, or L-dopa, is a drug that is converted to dopamine in the brain and is commonly used to treat the motor symptoms associated with loss of dopaminergic nerve cells in patients suffering from Parkinson's disease.

Cytokine-mediated inflammation

Published studies suggest that nicotine, acting upon specific NNRs, may modulate the inflammatory response by downregulating the production and release of cytokines, which are molecules that regulate inflammatory reactions. In addition, compounds that act selectively on the a7 NNR have been shown to be active in various preclinical models of inflammatory activity, including models of sepsis, rheumatoid arthritis and asthma. These findings support the targeting of NNRs in the development of treatments for cytokine-mediated inflammatory disorders.

Our Drug Discovery Technologies—Pentad

Our drug discovery activities utilize sophisticated proprietary computer-based molecular design methodologies and extensive biological and chemical data for a library of diverse compounds developed and collected over more than 20 years. We refer to these technologies collectively as Pentad. We use Pentad to predict the likelihood that novel compounds will interact with various NNRs, the degree of the interaction and the potential of these compounds to be developed as drugs based on projected pharmacokinetic profiles.

Pentad's virtual screening facilitates more rapid identification and prioritization of compounds that may be clinically viable than we believe could be achieved using traditional laboratory synthesis and screening methods. This allows us to reduce drug development time by focusing our resources on compounds believed to have a greater likelihood of clinical success.

Discontinued Product

As a result of increased fees charged by the United States Food and Drug Administration, or FDA, and declining prescriptions, we discontinued Inversine, which is currently our only approved product, effective as of September 30, 2009. Inversine is approved in the United States for the management of moderately severe to severe essential hypertension and uncomplicated cases of malignant hypertension, which are high blood pressure disorders. Inversine has been approved for marketing since the 1950s, and we acquired marketing rights to the product in August 2002 from Layton Bioscience, Inc., which had previously acquired the rights from Merck & Co., Inc.

Strategic Alliances and Collaborations

AstraZeneca AB – TC-5214

On December 3, 2009, we entered into a collaboration and license agreement with AstraZeneca AB for the global development and commercialization of TC-5214. The agreement became effective later in December. Pursuant to the agreement, we granted AstraZeneca an exclusive global license under patents and other technology owned or licensed by us to develop and commercialize TC-5214, as well as any other compounds of ours that meet specified structural and pharmacological criteria designed to reflect substantial similarity to TC-5214, for all fields of use except hypertension.

Payment Terms. In January 2010, AstraZeneca made a non-refundable upfront payment of $200 million, which was triggered upon the agreement becoming effective. The agreement provides for us to be eligible to receive up to an additional $540 million if specified development, regulatory and first commercial sale milestones are achieved, up to an additional $500 million if specified sales-related milestones are achieved, and significant stepped double digit royalties on any future product sales. Under the terms of an existing license agreement, we paid $16 million to University of South Florida Research Foundation, or USFRF, based on our receipt of the upfront payment from AstraZeneca and, if we receive any milestone payments from AstraZeneca under the agreement, we would be required to pay a percentage of each such milestone payment, after deducting the unexhausted portion of our projected share of the costs of the initial development program for TC-5214, as well as royalties on any future product sales, to USFRF. The percentage of each milestone payment, net of any deduction, that we would be required to pay would be at least 10% and could be greater in specified circumstances. Based on the terms of the license agreement with USFRF and the terms of another existing license agreement with Yale University, we expect to pay royalties at an effective worldwide rate in the low single digits and such effective royalty rate could in some circumstances reach the mid single digits.

AstraZeneca's obligation to pay royalties to us for TC-5214 expires on a country-by-country basis on the later of expiration of the patent rights in each country licensed by us to AstraZeneca that have a specified scope or 12 years after the first commercial sale of TC-5214 in that country. The U.S. patent rights with respect to TC-5214 licensed by us to AstraZeneca expire between 2017 and 2020 and the corresponding licensed foreign patent rights licensed by us to AstraZeneca expire between 2017 and 2019. We have also licensed to AstraZeneca pending U.S. and foreign patent applications with respect to TC-5214 that, if issued as patents, would expire between 2019 and 2030. None of the foregoing years of expiration reflect any patent term extension that may be available in a particular country. It is uncertain whether any of the pending U.S. and foreign patent applications, even if issued as a patent, would be sufficient to extend our royalty term under the agreement for TC-5214 in any particular country. Royalty rates are subject to reduction under the agreement in specified circumstances, including in any country if TC-5214 is not subject to patent protection with a specified scope in that country or if AstraZeneca licenses patent rights from any third party under circumstances in which it is more likely than not that TC-5214 would infringe the third party's patent rights.

Development and Commercialization. The agreement provides for us and AstraZeneca to co-develop TC-5214 under the oversight of a committee comprised of representatives of each company. The initial global clinical program is planned to include development of TC-5214 as an adjunct (or add-on) to antidepressant therapy and as a second-line "switch" monotherapy, in each case in adults with major depressive disorder who do not respond adequately to first-line antidepressant treatment. AstraZeneca is responsible for 80% of the costs of the initial program, except that AstraZeneca is responsible for 100% of development costs that are required only to obtain or maintain regulatory approval in countries outside the United States and the European Union. We are responsible for 20% of the costs of the initial program but have the right to terminate our obligation to fund our share of these costs once we have funded a specified amount. If we fund the specified amount and terminate our obligation to fund our share of further costs of the initial development program, any future milestones and royalties payable to us under the agreement would be reduced by the amount of our unfunded share plus interest, subject to a maximum reduction that may be applied to any one payment. In addition, if we and AstraZeneca mutually agree to develop TC-5214 for any indication other than major depressive disorder or in any formulation other than those contemplated by the initial program, the same cost sharing arrangement would apply, except that we would have the immediate right to terminate our obligation to fund our share of development costs for the other indication or formulation. If we terminate our obligation to fund our share of these other development costs, any future milestones and royalties payable to us under the agreement would be reduced by the amount of our unfunded share plus interest, subject to a maximum reduction that may be applied to any one payment, but only from and after the occurrence of a specified event to be agreed upon by both parties (e.g., receipt of regulatory approval of the applicable indication or formulation).

AstraZeneca is responsible under the agreement for executing and funding the costs of global commercialization of TC-5214, and we have retained an option to co-promote TC-5214 to a specified target

physician audience in the United States. If we exercise our co-promotion option, AstraZeneca would compensate us on a per detail basis. AstraZeneca is also responsible under the agreement for the manufacture and supply of TC-5214 and has assumed our rights and obligations under our applicable agreements with third parties.

Restrictions. For a three-year period beginning upon effectiveness of the agreement, neither we nor AstraZeneca is permitted to conduct, or to grant a license to any third party to conduct, a Phase 2 or later clinical trial, or to commercialize, a compound as an adjunct (or add-on) to antidepressant treatment for major depressive disorder, subject to certain exceptions that include, among others, AstraZeneca's right to develop and commercialize quetiapine (marketed by AstraZeneca as Seroquel XR) and other atypical antipsychotic products that meet a specified condition.

AstraZeneca has agreed under the agreement not to take specified actions with respect to acquiring control of us without our consent for a specified period. These restrictions, which cease to apply in various circumstances, do not preclude AstraZeneca from making confidential proposals that do not require us to make a public disclosure.

Termination. AstraZeneca can terminate the agreement in its entirety: within a specified period following completion of the Phase 3 development program for TC-5214 as an adjunct therapy; or if AstraZeneca determines there to be a serious safety issue regarding the continued development or commercialization of TC-5214; or if, having obtained the advice of independent patent counsel, AstraZeneca believes that the commercialization of TC-5214 is more likely than not to infringe or misappropriate intellectual property rights of third parties in the United States or any two specified major pharmaceutical markets and is unable to obtain a license on commercially reasonable terms. In addition, AstraZeneca can terminate the agreement on a major pharmaceutical market by major pharmaceutical market basis at any time beginning four years after effectiveness of the agreement, except that, if AstraZeneca terminates the agreement with respect to the United States, the agreement will terminate in its entirety. We can terminate the agreement if AstraZeneca or any of its affiliates or sublicensees challenges the validity or enforceability of any of the patent rights licensed to AstraZeneca. Either party can terminate the agreement in the event of the insolvency or uncured material breach of the other party. However, if an uncured material breach by AstraZeneca is limited to a specified major pharmaceutical market, we can terminate the agreement only with respect to that market. The rights and obligations of the parties that survive termination of the agreement, including license grants and payment obligations, vary depending on the basis for the termination.

In addition, in the event of a change of control of us, AstraZeneca can terminate specified provisions of the agreement, including our right to participate on the committee overseeing development under the agreement and our co-promotion rights.

AstraZeneca AB – Cognitive Disorders

In December 2005, we entered into a collaborative research and license agreement with AstraZeneca AB under which we granted AstraZeneca exclusive development and worldwide commercialization rights to AZD3480 as a treatment for specified conditions characterized by cognitive impairment, including ADHD, Alzheimer's disease, cognitive dysfunction in schizophrenia, AAMI, MCI and any other indication that is deemed a cognitive disorder under the agreement, as well as schizophrenia. The agreement became effective in January 2006.

In 2009, we and AstraZeneca completed a Phase 2 clinical trial of AZD3480 in adults with ADHD. Previously, we or AstraZeneca had completed clinical trials of AZD3480 in various indications characterized by cognitive impairment, including Alzheimer's disease, cognitive dysfunction in schizophrenia, age associated memory impairment and mild cognitive impairment. We expect AstraZeneca to conduct future clinical development of AZD3480 in ADHD. Whether additional development of AZD3480 will be conducted in the future in Alzheimer's disease or any other indication is uncertain.

We and AstraZeneca conducted a multi-year preclinical research collaboration under the agreement. The term of the research collaboration expired in January 2010. AZD1446 is the most advanced compound that arose from the research collaboration. AstraZeneca has completed multiple Phase 1 clinical trials of AZD1446, and AZD1446 is planned for further development as a treatment for either or both of Alzheimer's disease and ADHD.

As a result of a process that we initiated under the agreement and a related election made by AstraZeneca, TC-5619 is also subject to the agreement. We have agreed to develop TC-5619 independently through a Phase 2 clinical proof of concept trial pursuant to an agreed development plan. Following our completion of the development plan, AstraZeneca has the right to license TC-5619 and to further develop and potentially commercialize TC-5619 for various conditions characterized by cognitive impairment and on terms specified in the agreement.

Payment Terms. AstraZeneca paid us an initial fee of $10 million in February 2006, an additional $20 million in January 2007 as a result of its December 2006 determination to proceed with further development of AZD3480 and an additional $10 million in July 2009 as a result of the achievement of the objective in the Phase 2 clinical trial of AZD3480 in adults with ADHD. We are eligible to receive other payments of up to $103 million if development, regulatory and first commercial sale milestones for AZD3480 are achieved only for ADHD, and stepped double-digit royalties on any future AZD3480 product sales for any indication. We are also eligible to receive other payments if Alzheimer's disease becomes a target indication for further development of AZD3480 and development, regulatory and first commercial sale milestones for AZD3480 are achieved for Alzheimer's disease. The aggregate amount of contingent milestone payments that we are eligible to receive with respect to Alzheimer's disease and ADHD is $197 million. If AZD3480 is developed under the agreement for an indication in addition to Alzheimer's disease and ADHD, we would also be eligible to receive payments of up to $52 million, contingent upon the achievement of development, regulatory, first commercial sale and first detail milestones for AZD3480 for each such indication. Under the terms of a sponsored research agreement and a subsequent license agreement between us and University of Kentucky Research Foundation, or UKRF, if we receive any of these payments from AstraZeneca relating to AZD3480, including royalties, we are required to pay a low single digit percentage of each such payment to UKRF.

With respect to AZD1446, AstraZeneca has paid us $2.2 million upon the achievement of development and regulatory milestones. We are also eligible to receive other payments of up to $108 million, contingent upon the achievement of development, regulatory, first commercial sale and first detail milestones for AZD1446 for two indications, and stepped royalties on any future AZD1446 product sales.

If TC-5619 achieves clinical proof of concept and AstraZeneca licenses TC-5619, the agreement provides for AstraZeneca to make a $40 million payment to us. In that event, we would be eligible to receive additional payments of up to $226 million, contingent upon the achievement of development, regulatory and first commercial sale milestone events for three indications, as well as stepped double-digit royalties on any future product sales. If TC-5619 does not achieve Phase 2 clinical proof of concept but AstraZeneca remains interested in a potential license, the agreement provides for us and AstraZeneca to negotiate terms.

AstraZeneca's obligation to pay royalties to us for each compound subject to the collaboration expires on a country-by-country basis on the later of expiration of our patent rights that provide exclusivity for that compound in that country or 12 years after the first commercial sale in that country of either that compound or any related compound that meets specified criteria. If AstraZeneca obtains a patent covering the composition of a compound that is derived within a specified period from a compound that is subject to the collaboration, the term of AstraZeneca's patent would also be taken into account in determining the term of AstraZeneca's obligation to pay royalties to us for that derived compound. The U.S. patent rights with respect to AZD3480 expire between 2016 and 2026. The foreign patent rights with respect to AZD3480 that have issued and correspond to our issued U.S. patent rights expire between 2017 and 2019. We also have pending U.S. and foreign patent applications with respect to AZD3480 that, if issued as patents, would expire between 2017 and 2029. The U.S. patent rights

to the chemical genus that includes TC-5619 expire in 2019. The foreign patent rights to the chemical genus that includes TC-5619 corresponding to our issued U.S. patent rights expire in 2024. We also have a pending U.S. patent application with respect to TC-5619 specifically and to a particular salt form of TC-5619 that, if issued as patents, would expire in 2028. In addition, we have pending U.S. and foreign patent applications with respect to AZD1446 that, if issued as patents, would expire in 2027. None of the foregoing years of expiration reflect any patent term extension that may be available in a particular country. It is uncertain whether any of the pending U.S. and foreign patent applications, even if issued as a patent, would be sufficient to extend our royalty term under the agreement for AZD3480, AZD1446 or, if licensed by AstraZeneca, TC-5619 in any particular country. Royalty rates are subject to reduction under the agreement in specified circumstances, including in any country if the licensed compound is no longer subject to adequate patent protection in that country or if AstraZeneca licenses patent rights from any third party under circumstances in which the product that we license to AstraZeneca might infringe the third party's patent rights.

Research Collaboration and Fees. The agreement provides for a research collaboration that we and AstraZeneca conducted between January 2006 and January 2010 to discover and develop additional compounds that act on the a4ß2 NNR as treatments for conditions characterized by cognitive impairment. Under the agreement, AstraZeneca paid us research fees based on an agreed reimbursement rate for research services rendered by us in the collaboration. AstraZeneca has exclusively licensed six of these compounds, including AZD1446, together with metabolites of these compounds and derivatives and other compounds related to these compounds that meet specified criteria, for the same indications for which AstraZeneca has development and commercialization rights for AZD3480. Under the agreement, for each licensed compound that was discovered and developed as part of the research collaboration, we are eligible to receive additional contingent milestone payments and stepped royalties on any future product sales.

Development and Commercialization Costs. AstraZeneca is responsible for the clinical development and commercialization of AZD3480, AZD1446 and any other licensed compounds that arose from the research collaboration that it elects to advance and for funding substantially all future development costs. We have the option to co-promote AZD3480, AZD1446 and any other licensed compounds that arose from the research collaboration that are selected for advancement to specified classes of specialist physicians in the United States. If we exercise our co-promotion option, AstraZeneca is required to provide training to our sales force and compensate us for our detailing efforts following regulatory approval. If AstraZeneca licenses TC-5619, it would assume responsibility for and fund all future development and commercialization of TC-5619.

Exclusivity Rights and Restrictions. Neither we nor AstraZeneca are permitted outside of the collaboration to develop or commercialize compounds that act on the a4ß2 NNR and meet pre-defined criteria for ADHD, Alzheimer's disease, cognitive dysfunction in schizophrenia or other conditions characterized by cognitive impairment for which AstraZeneca has development and commercialization rights under the agreement or schizophrenia. This restriction on AstraZeneca lapses 30 months after January 2010. This restriction on us will lapse if AstraZeneca commences clinical development outside of the collaboration for a compound that acts on the a4ß2 NNR and meets pre-defined criteria.

With respect to any compound that meets pre-defined criteria for any NNR other than the a4ß2 NNR, at the time the compound has completed the preclinical testing necessary to conduct clinical development, we are entitled to offer to AstraZeneca the right to develop and commercialize it for any indication for which AstraZeneca has development and commercialization rights under the agreement. As an example, we made such an offer with respect to TC-5619, which led to AstraZeneca's future right to license TC-5619. If we do not offer this right to AstraZeneca for a compound that meets pre-defined criteria for any NNR other than the a4ß2 NNR, we are generally not permitted to develop or commercialize the compound for any indication for which AstraZeneca has development and commercialization rights under the agreement.

If we offer a compound to AstraZeneca, AstraZeneca could license the compound from us, together with metabolites of the compound and derivatives and other compounds related to the compound that meet specified criteria, on terms specified in the agreement. Alternatively, as in the case of TC-5619, AstraZeneca could

negotiate a development plan with us pursuant to which we would conduct development intended to provide a pre-defined indication of efficacy. AstraZeneca could license the compound from us after we complete the additional development. For each compound licensed by AstraZeneca through this process, we are eligible to receive an exercise fee and other payments contingent upon the achievement of development, regulatory, first commercial sale and first detail milestones, as well as stepped royalties on any future product sales. If AstraZeneca elects not to license the compound, we are permitted to develop and commercialize the compound for any indication, except that, if we had offered the compound to AstraZeneca for schizophrenia, we will not be able to develop or commercialize the compound for any cognitive disorder. The agreement limits the number of compounds that we are permitted to offer to AstraZeneca through this process. We are generally not permitted to develop or commercialize compounds that meet pre-defined criteria for any NNR for any indication for which AstraZeneca has development and commercialization rights under the agreement except through this process.

We are also entitled to offer to AstraZeneca the right to develop and commercialize (1) any compound for which AstraZeneca has development and commercialization rights for specified indications under the agreement, or (2) any other compound that meets pre-defined criteria for cognitive activity, is in the same chemical family and acts on the same NNR or NNRs as any compound for which AstraZeneca has development and commercialization rights for specified indications under the agreement, for any indication for which AstraZeneca does not have development and commercialization rights under the agreement. If we do not offer this right to AstraZeneca, we are not permitted to develop or commercialize the compound.

If AstraZeneca commences clinical development outside of the collaboration of a compound that acts on any NNR other than the a7 NNR and meets other pre-defined criteria, the restriction on our right to develop and commercialize compounds that meet pre-defined criteria for any NNR, other than the a4ß2 NNR, for any indication for which AstraZeneca has development and commercialization rights under the agreement will lapse.

If we seek a strategic collaborator to develop or commercialize compounds that act by binding to NNRs for depression, anxiety or bipolar disorder, AstraZeneca may under certain circumstances have a right of first negotiation with us. If AstraZeneca is interested in such a collaboration but we and AstraZeneca do not agree on terms on which we would collaborate, for the following three years we would only be permitted to enter into a collaboration for the applicable compounds and indications on more favorable terms than the terms offered by AstraZeneca.

Termination. AstraZeneca can terminate the agreement without cause upon 90 days notice given any time. Either we or AstraZeneca can terminate the agreement in the event of the bankruptcy or uncured material breach of the other party. However, if a breach by AstraZeneca is limited to any specific compound or specified major pharmaceutical market, we can terminate the agreement only with respect to that compound or major pharmaceutical market. If a competitor of AstraZeneca acquires control of us, AstraZeneca can terminate the agreement or specified provisions of the agreement, including our right to participate on the committee overseeing development under the agreement and our co-promotion rights.

GlaxoSmithKline

On July 27, 2007, we entered into a product development and commercialization agreement with GlaxoSmithKline that sets forth the terms of an alliance designed to discover, develop and market product candidates that selectively target specified NNR subtypes in five therapeutic focus areas—pain, smoking cessation, addiction, obesity and Parkinson’s disease. GlaxoSmithKline is participating in the alliance through its Center of Excellence for External Drug Discovery, or CEEDD.

In February 2010, GlaxoSmithKline announced plans to cease discovery research in selected neuroscience areas, specifically including pain. Discussions with GlaxoSmithKline regarding the effects of its strategic change on our alliance are ongoing. Until these discussions are completed, the overall impact is uncertain, but we currently anticipate that multiple therapeutic focus areas in the alliance will be discontinued. Because the overall impact has not yet been determined, the remainder of this discussion describes the current terms of the alliance.

Research and Early Development. Under the agreement, we have agreed, for specified periods of time and at our sole expense, to use diligent efforts to conduct research activities designed to discover product candidates that target specified NNR subtypes, to develop the product candidate identified as the lead for each therapeutic focus area through a Phase 2 clinical proof of concept trial and to develop up to two other product candidates for each therapeutic focus area to a specified stage of preclinical development. We are eligible to receive contingent milestone payments from GlaxoSmithKline as we advance product candidates in each therapeutic focus area through preclinical and Phase 1 clinical development. Our research and development activities in the alliance are overseen by a joint steering committee comprised of representatives of both us and GlaxoSmithKline.

Options; Later-Stage Development and Commercialization. With respect to each therapeutic focus area in the alliance, if we achieve clinical proof of concept with a lead product candidate, GlaxoSmithKline would have an exclusive option for an exclusive license to that lead product candidate and up to two other product candidates in development in the alliance for the same therapeutic focus area on a worldwide basis. If GlaxoSmithKline exercises its option and pays a non-refundable exercise fee, GlaxoSmithKline would become responsible for using diligent efforts to conduct later-stage development and commercialization of the lead product candidate at its sole expense. GlaxoSmithKline's exclusive license would include all fields of use other than those indications for which AstraZeneca has development and commercialization rights under our 2005 agreement with AstraZeneca.

Payment Terms. Upon execution of the agreement, GlaxoSmithKline made payments to us of $35 million, which included a non-refundable initial payment of $20 million and the purchase of 1,275,502 shares of our common stock for an aggregate purchase price of $15 million. As of February 28, 2010, we had received an additional $10 million based on achievement of discovery and development milestones under the agreement. We are also eligible to receive other payments, contingent on the achievement of specified discovery, development, regulatory and commercial milestones in each therapeutic focus area of the alliance, as well as stepped double-digit royalties on any sales achieved for products licensed by GlaxoSmithKline. The amounts that we are eligible to receive include up to $16 million in each therapeutic focus area, contingent upon the achievement of specified milestones prior to Phase 2 clinical proof of concept.

With respect to each product licensed from us by GlaxoSmithKline that, at the time of first commercial sale in a particular country, is covered by an issued Targacept patent with a scope that qualifies as royalty-bearing under the agreement, GlaxoSmithKline's royalty obligation with respect to sales of the product in the country generally would terminate upon the later of the expiration of the last Targacept patent with qualifying scope or 15 years after the first commercial sale of the product in the country. The royalty rate payable to us would be subject to reduction in specified circumstances under the agreement, including in any country if the product is no longer covered by a patent with qualifying scope under the agreement in that country or if GlaxoSmithKline licenses patent rights from any third party in circumstances in which such license is reasonably considered necessary to avoid the infringement of the third-party patent rights.

Exclusivity. We have agreed that, with respect to each of the therapeutic focus areas of the alliance, for so long as we are required under the agreement to conduct research activities in the therapeutic focus area or for so long thereafter as there are any product candidates in development or being commercialized in the alliance in the therapeutic focus area, we will work in the therapeutic focus area exclusively with GlaxoSmithKline with respect to product candidates with activity derived from binding to NNRs. We have also agreed to work exclusively with GlaxoSmithKline for a specified period of time with respect to product candidates with substantially the same mechanism of action, as defined in the agreement, as product candidates being developed or commercialized in the alliance. Some or all of our exclusivity obligations would expire if GlaxoSmithKline were to in-license from a third party a product candidate with NNR-derived activity for a therapeutic focus area of the alliance. GlaxoSmithKline has agreed for a specified period of time not to conduct internal activities for any of the alliance's therapeutic focus areas with respect to product candidates that target the NNR subtypes specified under the agreement for such therapeutic focus area.

Expiration and Termination. If GlaxoSmithKline does not exercise any of its options, or if we do not achieve clinical proof of concept in any of the therapeutic focus areas of the alliance within a specified period, the agreement would expire. Otherwise, the agreement would expire with respect to each licensed product and country upon the expiration of the payment obligations of GlaxoSmithKline for that licensed product in that country and would expire in its entirety upon the expiration of the last payment obligation of GlaxoSmithKline for the last licensed product in the last country.

Either we or GlaxoSmithKline have the right to terminate the agreement if the other party becomes insolvent or commits an uncured material breach of the agreement, except that, if the uncured material breach is of a party's diligence obligations with respect to a product candidate for a particular therapeutic focus area of the alliance, the other party's right is only to terminate the agreement as applied to that therapeutic focus area. GlaxoSmithKline also has the right to terminate the agreement without cause upon 90 days notice, either in its entirety or as to any particular therapeutic focus area. We also have the right to terminate the agreement as to any particular therapeutic focus area, if GlaxoSmithKline challenges the scope, validity or enforceability of certain patents that cover compounds in development in the alliance for that therapeutic focus area. In addition, the agreement can be terminated by us or any successor following a change of control of us that meets specified conditions, upon payment of a specified sum to GlaxoSmithKline and the grant to GlaxoSmithKline of a license to a specified number of product candidates then in development in each of the therapeutic focus areas of the alliance. The rights and obligations of each of us and GlaxoSmithKline that survive termination of the agreement, including license grants, product candidates to which the license grants would apply and payment obligations, vary depending on the basis of the termination.

Patents and Proprietary Rights

We actively seek to protect the proprietary technology that we consider important to our business, including chemical species, compositions and forms, their methods of use and processes for their manufacture, as well as modified forms of naturally-expressed receptors, in the United States and other jurisdictions internationally that we consider key pharmaceutical markets. We also rely upon trade secrets and contracts to protect our proprietary information.

As of February 28, 2010, our patent estate included 58 patents issued in the United States, 54 patent applications pending in the United States and over 550 counterpart patents and patent applications in countries other than the United States. Our issued patents and pending patent applications in the United States include composition of matter coverage on a number of different structural families of compounds. The actual protection afforded by a patent varies from country to country and depends upon many factors, including the type of patent, the scope of its coverage and the availability of legal remedies in a particular country.

We consider the following United States patents that we own or license to be particularly important to the protection of our most advanced product candidates.

Product Candidate	Patent Scope	Patent Expiration
TC-5214	Pharmaceutical composition of S-mecamylamine	January 2020
	Methods of use of S-mecamylamine for neuropsychiatric disorders, including depression	February 2020
AZD3480 (TC-1734)	Composition of matter for AZD3480 (TC-1734)	July 2018
	Composition of matter for a family of compounds that includes AZD3480 (TC-1734)	April 2016
	Methods of use of a family of compounds that includes AZD3480 (TC-1734) for treatment and prevention of CNS disorders	February 2017
	Composition of matter for the preferred salt (p-hydroxybenzoate) of AZD3480	August 2026
TC-5619	Composition of matter for a family of compounds that includes TC-5619	August 2019
	Composition of matter for a racemic mixture that includes TC-5619	March 2019
TC-6987	Composition of matter for a family of compounds that includes TC-6987	August 2019
TC-6499	Composition of matter for TC-6499; composition of matter for a family of compounds that includes TC-6499	February 2024
TC-5685	Composition of matter for TC-5685; composition of matter for a family of compounds that includes TC-5685	June 2023

In addition to these patents, for some of these product candidates we have later-expiring patents that cover a particular form or composition, use as part of combination therapy or method of preparation or use, as well as other pending patent applications. These issued patents, including any patents that issue from the pending applications, could provide additional or a longer period of protection. We also have patent applications pending that seek equivalent or substantially comparable protection for our product candidates in jurisdictions internationally that we consider key pharmaceutical markets.

The patent expiration dates referenced above do not reflect any potential patent term extension that we may receive under The United States Drug Price Competition and Patent Term Restoration Act of 1984, known as the Hatch-Waxman Act. The Hatch-Waxman Act generally permits a patent extension term of up to five years as compensation for patent term lost during the FDA regulatory review process. Patent extension cannot extend the remaining term of a patent beyond a total of 14 years. The patent term restoration period is generally one-half the time between the effective date of an investigational new drug application, or IND, and the submission date of a new drug application, or NDA, plus the time between the submission date and approval date of an NDA. Only one patent applicable to an approved drug is eligible for the extension, and the extension must be applied for prior to expiration of the patent. The United States Patent and Trademark Office, in consultation with the FDA, reviews and approves applications for patent term extension.

License Agreements

We consider the following license agreements to be important to our business.

University of South Florida Research Foundation

Pursuant to a license agreement with USFRF, we hold an exclusive worldwide license under patents and patent applications owned by USFRF to develop and commercialize TC-5214, mecamylamine hydrochloride and other specified compounds. The licensed patents and patent applications include issued patents covering the pharmaceutical composition of TC-5214 and methods of use of each of TC-5214, the other enantiomer of mecamylamine hydrochloride and mecamylamine hydrochloride for the treatment of various disorders, including major depressive disorder. We sublicensed rights under the licensed patents and patent applications to AstraZeneca pursuant to our 2009 agreement with AstraZeneca.

Under the license agreement with USFRF, we are obligated to pay to USFRF:

- an annual license fee until we or AstraZeneca or any future sublicensee files an NDA or foreign equivalent for use of a product subject to the license to treat a neuropsychiatric disease or disorder;
- an annual fee to maintain our right of first refusal to acquire rights under the licensed patents and patent applications beyond the scope of our current license;
- royalties on net sales of products subject to the license or, if less, a percentage of royalties that we receive from AstraZeneca or any future sublicensee;
- aggregate payments of up to $200,000 based on the achievement of specified regulatory milestones; and
- 10% of other amounts, including milestone payments, that we receive for a sublicense from AstraZeneca or any future sublicensee, subject to increase to a higher percentage in specified circumstances.

The aggregate annual license fees are creditable, up to a specified amount per year, against future royalties.

We are required to use commercially reasonable efforts to develop or to market and sell one or more products subject to the license. In particular, we are required to spend a specified minimum amount on research and development of products subject to the license over each consecutive three-year period during the term of the agreement until we or a sublicensee file an NDA or foreign equivalent for use of a product subject to the license to treat a neuropsychiatric disease or disorder. If USFRF believes that we are not meeting our diligence obligation, it is entitled to terminate the agreement following a cure period. If we do not agree with USFRF's determination and specified initial dispute resolution procedures are unsuccessful, we can submit the matter to binding arbitration.

We may terminate the agreement at any time. USFRF may terminate the agreement if we fail to make a required royalty payment when due, or commit a material breach of the agreement, and do not cure the failure or breach within specified cure periods. If not earlier terminated, the agreement will terminate upon expiration of the last to expire of the licensed patent rights that includes a valid claim.

Yale University

Pursuant to an exclusive license agreement with Yale University, we hold an exclusive worldwide license to pending patent applications owned by Yale. The licensed patent applications include a pending U.S. application that, if issued in the future as a patent, could potentially cover the use of TC-5214 and mecamylamine hydrochloride, or other compounds classified as nicotinic antagonists, as an augmentation to other treatments for mood disorders, including major depressive disorder. We sublicensed rights under the licensed patent applications to AstraZeneca pursuant to our 2009 agreement with AstraZeneca.

Under the license agreement with Yale, we are obligated to pay to Yale:

- an issuance fee that is conditional upon the issuance of a licensed patent in the United States that meets specified conditions;
- aggregate payments of up to $1.5 million for each product subject to the license for which specified regulatory and first commercial sale milestone events are achieved;
- royalties on net sales of products subject to the license, subject, following the first launch of a product subject to the license, to specified annual minimum amounts; and
- a percentage of other amounts received from AstraZeneca or any future sublicensee of the licensed patent rights if the applicable sublicense is not combined with a license to other patent rights owned or licensed by us or with an agreement by us to collaborate to discover, research, develop or commercialize compounds or products for therapeutic use in humans.

We are required to use reasonable commercial efforts to develop at least one product subject to the license for commercialization in the United States. We may terminate the agreement upon 30 days notice to Yale. Yale may terminate the agreement if we fail to make a required payment when due, or commit a material breach of the agreement, and do not cure the failure or breach within a specified cure period or if we notify Yale that we are finally abandoning our exploitation and intended exploitation of products subject to the license. If not earlier terminated, the agreement will expire upon expiration of the last to expire of the licensed patent rights that includes a valid claim.

University of Kentucky Research Foundation

Pursuant to a sponsored research agreement, UKRF agreed to assign to R.J. Reynolds Tobacco Company UKRF's rights to inventions that resulted in patents related to AZD3480. These patents were subsequently assigned by RJR to us in August 2000, and we licensed rights under these patents to AstraZeneca pursuant to our 2005 agreement with AstraZeneca. Under the sponsored research agreement and a subsequent license agreement with UKRF, we are obligated to pay royalties to UKRF based on amounts received for a license to these patents from AstraZeneca or any future licensee.

Trade Secrets

In addition to patents, we rely upon unpatented trade secrets and know-how and continuing technological innovation to develop and maintain our competitive position. For example, we maintain Pentad as an unpatented trade secret. We seek to protect our proprietary information, in part, by using confidentiality agreements with our commercial partners, collaborators, employees and consultants and invention assignment agreements with our employees.

Sales and Marketing

We currently have limited sales, marketing and distribution experience with respect to pharmaceutical products and no internal sales or distribution capabilities. Our current strategy is to selectively seek alliances and collaborations for target indications for which our potential collaborator has particular expertise or that involve large primary care markets that must be served by large sales and marketing organizations. In entering into these alliances and collaborations, our goal will generally be to maintain co-promotion or co-commercialization rights in the United States and, in some cases, other markets. In order to implement our strategy successfully, we must develop a specialized sales and marketing organization with sufficient technical expertise.

We discontinued Inversine, which is currently our only approved product, effective as of September 30, 2009. Inversine had been distributed by Cord Logistics, Inc., a Cardinal Health company, pursuant to an exclusive distribution agreement. We have terminated our agreement with Cord Logistics. We paid Cord Logistics approximately $140,000 in 2009, $170,000 in 2008 and $180,000 in 2007.

Manufacturing

All of our current product candidates are compounds of low molecular weight, commonly referred to as small molecules, that can be manufactured in a simple synthetic process from readily available starting materials. We expect to continue to develop product candidates that can be produced cost-effectively by third-party contract manufacturers.

We are able to manufacture the quantities of our product candidates necessary for relatively short preclinical studies ourselves. However, we do rely and expect to continue to rely on a number of contract manufacturers to produce enough of our product candidates for use in more lengthy preclinical research. We also depend on these contract manufacturers to manufacture our product candidates in accordance with current good manufacturing practices, or cGMP, for use in clinical trials. We will ultimately depend on contract manufacturers for the manufacture of our products for commercial sale, as well as for process development. Contract manufacturers are subject to extensive governmental regulation.

Competition

Our industry is subject to rapid and intense technological change. We face, and will continue to face, worldwide competition from biotechnology, biopharmaceutical and pharmaceutical companies, research institutions, government agencies and academic institutions.

We also face substantial competition from therapies designed to target NNRs. Pfizer's product Chantix, which is known outside of the United States as Champix, acts on several NNR subtypes as well as other molecular targets in the body. Chantix is approved as an aid for smoking cessation. In addition, we believe that several prominent pharmaceutical companies have product candidates that target NNRs in development, including as examples Roche, with a compound in Phase 2 development for Alzheimer's disease and cognitive impairment associated with schizophrenia (which we refer to as cognitive dysfunction in schizophrenia), and Abbott Laboratories, with one compound in Phase 2 development for Alzheimer's disease and ADHD, a second compound in Phase 2 development for ADHD and a third compound in Phase 1 development for cognitive disorders. Other companies that we believe have active NNR-based programs include AstraZeneca, Eli Lilly, Sanofi-Aventis, Wyeth, Bristol Myers Squibb, GlaxoSmithKline, Johnson & Johnson, Novartis, NeuroSearch A/S, Solvay, Servier, CoMentis, EnVivo Pharmaceuticals, Xytis and Galantos Pharma. We expect that we will face increased competition in the future if therapies that target NNRs are further validated and if companies initiate or expand programs focused on NNRs or otherwise enter the CNS market, whether independently or by alliance or acquisition.

In addition, there are several pharmaceutical companies in the United States and globally that currently market and sell drugs for indications that we are targeting. We believe that the primary competitive products for use in indications that we are currently targeting with our most advanced product candidates include:

- for major depressive disorder, selective serotonin reuptake inhibitors such as Prozac from Eli Lilly, Paxil/Seroxar from GlaxoSmithKline, Zoloft from Pfizer, Celexa and Lexapro from Forest Laboratories, dual uptake inhibitors such as Effexor from Wyeth and Cymbalta from Eli Lilly, and, as an adjunctive treatment, the atypical antipsychotics Seroquel XR from AstraZeneca and Abilify from Bristol-Myers Squibb/Otsuka;
- for ADHD, stimulants such as Adderall XR and Vyanase from Shire, Concerta from Johnson & Johnson and Ritalin LA from Novartis, and Strattera, a non-stimulant acting as a norepinephrine reuptake inhibitor, from Eli Lilly; and
- for mild to moderate Alzheimer's disease, acetylcholinesterase inhibitors such as Aricept from Pfizer/Eisai, Razadyne from Johnson & Johnson and Exelon from Novartis; in addition, Namenda from Forest Laboratories, which acts by regulating the neurotransmitter glutamate, is marketed for moderate to severe Alzheimer's disease.

There is currently no approved product for cognitive dysfunction in schizophrenia.

Many of these products have well-known brand names, are distributed by large pharmaceutical companies with substantial resources, have achieved widespread acceptance among physicians and patients and are or may become available in lower priced generic form. Furthermore, pharmaceutical, biopharmaceutical and biotechnology companies are currently developing additional treatments for the indications that we are targeting that may be approved for marketing and sale prior to any approval of our product candidates.

We expect to compete based upon, among other things, the efficacy and favorable side effect profiles of our products. Our ability to compete successfully will depend on our continued ability to attract and retain skilled and experienced scientific, clinical development and executive personnel, to identify and develop viable product candidates into products and to exploit these products commercially before others are able to develop competitive products. In addition, our ability to compete may be affected by insurers and other third-party payors favoring the use of lower priced generic products over branded products.

Regulatory Matters

Government Regulation and Product Approval

Government authorities in the United States, at the federal, state and local level, and in other countries extensively regulate, among other things, the research, development, testing, manufacture, quality control, approval, labeling, packaging, storage, record-keeping, promotion, advertising, distribution, marketing and export and import of drugs such as those we are developing. Our product candidates must be approved by the FDA through the NDA process before they may be legally marketed in the United States.

United States Drug Development Process

In the United States, the FDA regulates drugs under the Federal Food, Drug, and Cosmetic Act, or FDCA, and implementing regulations. The process of obtaining regulatory approvals and the subsequent compliance with appropriate federal, state, local and foreign laws and regulations require the expenditure of substantial time and financial resources. Failure to comply with the applicable United States requirements at any time during the product development process, the approval process or after approval may subject an applicant to administrative or judicial sanctions. These sanctions could include the FDA's refusal to approve pending applications, withdrawal of an approval, a clinical hold, warning letters, product recalls, product seizures, total or partial suspension of production or distribution injunctions, fines, refusals of government contracts, restitution, disgorgement, or civil or criminal penalties.

The process required by the FDA before a drug may be marketed in the United States generally involves the following:

- completion of preclinical laboratory tests, animal studies and formulation studies conducted in accordance with Good Laboratory Practices or other applicable regulations;
- submission to the FDA of an IND, which must become effective before human clinical trials may begin;
- performance of adequate and well-controlled human clinical trials conducted in accordance with the regulations and guidelines establishing good clinical practices to establish the safety and efficacy of the drug for its intended use;
- submission to the FDA of an NDA in a form and content that the FDA deems to be acceptable for filing;
- satisfactory completion of an FDA inspection of the manufacturing facility or facilities at which the drug is produced to assess compliance with cGMP in order to assure that the facilities, methods and controls are adequate to preserve the drug's identity, strength, quality and purity; and
- FDA review and approval of the NDA.

The testing and approval process requires substantial time, effort and financial resources.

Once a drug is identified for development it enters the preclinical testing stage. Preclinical tests include laboratory evaluations of chemistry, toxicity and formulation, as well as animal studies. An IND sponsor must submit the results of the preclinical tests, together with manufacturing information and analytical data, to the FDA as part of the IND. The sponsor also includes a protocol detailing, among other things, the objectives of the first clinical trial, the parameters to be used in monitoring safety and, if the first trial lends itself to an efficacy evaluation, the efficacy criteria to be evaluated. Some non-clinical testing may continue even after the IND is submitted. The IND automatically becomes effective 30 days after receipt by the FDA, unless within the 30-day time period the FDA places the clinical trial on a clinical hold. In such a case, the sponsor and the FDA must resolve any outstanding concerns before the clinical trial can begin. Clinical holds also may be imposed by the FDA at any time before or during studies due to safety concerns or non-compliance with applicable law or regulation.

All clinical trials must be conducted under the supervision of one or more qualified investigators in accordance with the regulations and guidelines establishing good clinical practice. These regulations include the requirement that all research subjects provide informed consent. Further, an institutional review board, or IRB, must review and approve the plan for any clinical trial before it commences at any institution. An IRB considers, among other things, whether the risks to individuals participating in the trials are minimized and reasonable in relation to the anticipated benefits. The IRB also approves the information regarding the trial and the consent form that must be provided to each trial subject or his or her legal representative and must monitor the study until completed.

Each new clinical protocol must be submitted to the IND for FDA review and to the applicable IRBs for approval. Protocols detail, among other things, the objectives of the study, dosing procedures, subject selection and exclusion criteria, and the parameters to be used to monitor subject safety.

Clinical trials are typically conducted in three sequential phases that may overlap or be combined:

- *Phase 1:* Involves one or more clinical trials in healthy volunteers to evaluate safety, dosage tolerance, absorption, metabolism, distribution and excretion. In the case of some drugs for severe or life-threatening diseases, the initial human testing may be conducted in patients, particularly where the drug may be too inherently toxic to administer ethically to healthy volunteers;
- *Phase 2:* Involves one or more clinical trials in a limited patient population to identify possible adverse effects and safety risks, to evaluate preliminarily the efficacy of the drug for specific targeted diseases and to determine dosage tolerance and optimal dosage; and
- *Phase 3:* Involves one or more clinical trials to further evaluate dosage, clinical efficacy and safety in an expanded patient population at geographically dispersed study sites. These trials are intended to establish the overall risk-benefit ratio of the drug and provide, if appropriate, an adequate basis for product labeling.

Progress reports detailing the results of clinical trials must be submitted at least annually to the FDA and safety reports must be submitted to the FDA and the investigators for serious and unexpected adverse events. Any Phase 1, Phase 2 and Phase 3 trial may not be completed successfully within any specified period, or at all. The FDA or the sponsor may suspend a clinical trial at any time on various grounds, including a finding that the research subjects or patients are being exposed to an unacceptable health risk. Similarly, an IRB can suspend or terminate approval of a clinical trial at its institution if the clinical trial is not being conducted in accordance with the IRB’s requirements or if the drug has been associated with unexpected serious harm to patients.

Concurrent with clinical trials, companies usually complete additional animal studies and must also develop additional information about the chemistry and physical characteristics of the drug and finalize a process for manufacturing the drug as a product in commercial quantities in accordance with cGMP requirements. The

manufacturing process must be capable of consistently producing quality batches of the drug, and, among other things, the manufacturer must develop methods for testing the identity, strength, quality and purity of the final product. Additionally, appropriate packaging must be selected and tested and stability studies must be conducted to demonstrate that the product does not undergo unacceptable deterioration over its shelf life.

U.S. Review and Approval Processes

The results of product development, preclinical studies and clinical trials, along with descriptions of the manufacturing process, analytical chemistry tests, proposed labeling, and other relevant information, are submitted to the FDA as part of an NDA requesting approval to market the drug as a product. The submission of an NDA is subject to the payment of user fees. A waiver of such fees may be obtained under specified limited circumstances.

In addition, under the Pediatric Research Equity Act, or PREA, an NDA or supplement to an NDA must contain data to assess the safety and effectiveness of the drug for the claimed indications in all relevant pediatric subpopulations and to support dosing and administration for each pediatric subpopulation for which the drug is safe and effective. The FDA may grant deferrals for submission of data or full or partial waivers. Unless otherwise required by regulation, PREA does not apply to any drug for an indication for which orphan designation has been granted.

The FDA reviews all NDAs submitted to ensure that they are sufficiently complete for substantive review before it accepts them for filing. The FDA has 60 days from its receipt of an NDA to determine if it will accept the submission for a substantive review, which is referred to as accepting it for filing. The FDA may request additional information rather than accept an NDA for filing. In this event, the NDA must be resubmitted with the additional information. The resubmitted application also is subject to review before the FDA accepts it for filing. The FDA may refuse to file the NDA. If the submission is accepted for filing, the FDA begins an in-depth substantive review to determine, among other things, whether a product is safe and effective for its intended use and whether its manufacturing is cGMP-compliant to assure and preserve the product's identity, strength, quality and purity. In that regard, the FDA will inspect the facility or facilities where the product is manufactured before approving an NDA.

Under current performance goals, the FDA has either six or 10 months to review and act on the NDA, depending upon whether the NDA is classified by the FDA as eligible for priority or standard review. The FDA often extends the review timeline by requesting additional information or clarification. The FDA may refer the NDA to an advisory committee for review, evaluation and a recommendation as to whether the application should be approved and under what conditions. The FDA is not bound by the recommendation of an advisory committee, but often follows the recommendation.

The FDA approval process is lengthy and difficult and the FDA may refuse to approve an NDA if the applicable regulatory criteria are not satisfied or may require additional clinical or other data and information. Even if any requested additional data or information is submitted, the FDA may ultimately decide that the NDA does not satisfy the criteria for approval. Data obtained from clinical trials are not always conclusive and the FDA may interpret data differently than we or any collaborator of ours does. The FDA may issue an approvable letter, which may require additional clinical or other data or impose other conditions that must be met in order to secure final approval of the NDA.

NDAs receive either standard or priority review. A drug representing a significant improvement in treatment, prevention or diagnosis of disease may receive priority review. In addition, products studied for their safety and effectiveness in treating serious or life-threatening illnesses and that provide meaningful therapeutic benefit over existing treatments may receive accelerated approval and may be approved on the basis of adequate and well-controlled clinical trials establishing that the drug has an effect on a surrogate endpoint that is reasonably likely to predict clinical benefit or on the basis of an effect on a clinical endpoint other than survival

or irreversible morbidity. As a condition of approval, the FDA may require that a sponsor of a drug receiving accelerated approval perform adequate and well-controlled post-marketing clinical trials. Priority review and accelerated approval do not change the standards for approval, but may expedite the approval process.

If a drug receives regulatory approval for marketing as a product, the approval may be limited to specific diseases and dosages, or the indications for use may otherwise be limited, which could restrict its commercial value. In addition, the FDA may require after NDA approval Phase 4 testing, which involves clinical trials designed to further assess a drug's safety and effectiveness, or testing and surveillance programs to monitor the safety of approved products that have been commercialized.

If a drug is the subject of an approved NDA, it may become a listed drug that can, in turn, be cited by potential competitors in support of approval of an abbreviated new drug application, or ANDA. An ANDA provides for marketing of a drug product that is therapeutically equivalent to a marketed listed drug. This means, among other things, that it has the same active ingredient(s), route of administration, dosage form and strength, as well as the same labeling, with certain exceptions, and the labeling must prescribe conditions of use that have been previously approved for the listed drug. If the generic drug product has a different route of administration, dosage form, or strength, the FDA must grant a suitability petition approving the difference(s) from the listed drug before the ANDA may be filed. The ANDA must also contain data and information demonstrating that the generic drug product is bioequivalent to the listed drug or, if the application is submitted pursuant to an approved suitability petition, information to show that the listed drug and the generic drug product can be expected to have the same therapeutic effect as the listed drug when administered to patients for a proposed condition of use. There is generally no requirement, other than the requirement for evidence of bioequivalence, for an ANDA applicant to conduct or submit results of preclinical tests or clinical trials to establish the safety or efficacy of its generic drug product. Drugs approved in this way are commonly referred to as generic equivalents to the listed drug, are listed as such by the FDA and can typically be substituted by pharmacists under prescriptions written for the original listed drug.

Marketing Exclusivity

Market exclusivity provisions under the FDCA also can delay the submission or the approval of certain applications. The FDCA provides a five-year period of non-patent marketing exclusivity within the United States to the first applicant to gain approval of an NDA for a new chemical entity. A drug is a new chemical entity if the FDA has not previously approved any other drug containing the same active moiety, which is the molecule or ion responsible for the action of the drug. During the exclusivity period, the FDA may not accept for review an ANDA or an NDA under Section 505(b)(2) of the FDCA submitted by another company for another version of such drug where the applicant does not own or have a legal right of reference to all the data required for approval. However, an application may be submitted after four years if it contains a certification of patent invalidity or non-infringement. The FDCA also provides three years of marketing exclusivity for an NDA, Section 505(b)(2) NDA or supplement to an existing NDA if new clinical investigations, other than bioavailability studies, conducted or sponsored by the applicant are deemed by the FDA to be essential to the approval of the application, for example, for new indications, dosages, or strengths of an existing drug. This three-year exclusivity covers only the conditions associated with the new clinical investigations and does not prohibit the FDA from approving ANDAs for drugs containing the original active agent. Five-year and three-year exclusivity will not delay the submission or approval of a full NDA; however, an applicant submitting a full NDA would be required to conduct or obtain a right of reference to all of the preclinical studies and adequate and well-controlled clinical trials necessary to demonstrate safety and effectiveness.

Pediatric exclusivity is another type of exclusivity in the United States. Pediatric exclusivity, if granted, provides an additional six months to an existing exclusivity or statutory delay in approval resulting from a patent certification. This six-month exclusivity, which runs from the end of other exclusivity protection or patent delay, may be granted based on the voluntary completion of a pediatric study in accordance with an FDA-issued "Written Request" for the study.

Orphan Drug Designation

Under the Orphan Drug Act, the FDA may grant orphan drug designation to a drug intended to treat a rare disease or condition, which is generally a disease or condition that either affects fewer than 200,000 individuals in the United States or affects more than 200,000 individuals in the United States but for which there is no reasonable expectation that the cost of developing and making available in the United States a drug for the disease or condition will be recovered from sales in the United States for that drug. Orphan drug designation must be requested before submitting an NDA. After the FDA grants orphan drug designation, the identity of the therapeutic agent and its potential orphan use are disclosed publicly by the FDA. Orphan drug designation does not convey any advantage in or shorten the duration of the regulatory review and approval process.

If a product that has orphan drug designation subsequently receives the first FDA approval for the disease for which it has such designation, the product is entitled to orphan product exclusivity, which means that the FDA may not approve any other applications to market the same drug for the same indication, except in very limited circumstances, for seven years.

The FDA also administers a clinical research grants program, whereby researchers may compete for funding to conduct clinical trials to support the approval of drugs, biologics, medical devices, and medical foods for rare diseases and conditions. A drug does not have to be designated as an orphan drug to be eligible for the grant program. An application for an orphan grant proposes one discrete clinical study to facilitate FDA approval of the product for a rare disease or condition. The study may address an unapproved new product or an unapproved new use for a product already on the market.

Post-Approval Requirements

Once an approval is granted, the FDA may withdraw the approval if compliance with regulatory standards is not maintained or if problems occur after the product reaches the market. Later discovery of previously unknown problems with a product may result in restrictions on the product or even complete withdrawal of the product from the market. After approval, some types of changes to the approved product, such as adding new indications, manufacturing changes and additional labeling claims, are subject to further FDA review and approval. Drug manufacturers and other entities involved in the manufacture and distribution of approved drugs are required to register their establishments with the FDA and certain state agencies and are subject to periodic unannounced inspections by the FDA and certain state agencies for compliance with cGMP and other laws.

Any products manufactured or distributed by us pursuant to FDA approvals are subject to continuing regulation by the FDA, including, among other things, record-keeping requirements, reporting of adverse experiences with the drug, providing the FDA with updated safety and efficacy information, drug sampling and distribution requirements, complying with certain electronic records and signature requirements, and complying with FDA promotion and advertising requirements. The FDA strictly regulates labeling, advertising, promotion and other types of information on products on the market. Products may be promoted only for the approved indications and in accordance with the provisions of the approved label.

From time to time, legislation is drafted, introduced and passed by the U.S. Congress that could significantly change the statutory provisions governing the approval, manufacturing and marketing of products regulated by the FDA. For example, the Food and Drug Administration Amendments Act of 2007, or FDAAA, gives the FDA the authority to require post-market studies and clinical trials, labeling changes based on new safety information and compliance with a risk evaluation and mitigation strategy approved by the FDA. Failure to comply with any requirements under FDAAA may result in significant penalties. FDAAA also authorizes significant civil money penalties for the dissemination of false or misleading direct-to-consumer advertisements, allows the FDA to require companies to submit direct-to-consumer television drug advertisements for FDA review prior to public dissemination and expands the clinical trial registry so that sponsors of all clinical trials, except for Phase 1 trials, are required to submit certain clinical trial information for inclusion in the clinical trial registry data bank. In addition to the impact of new legislation, FDA regulations and guidance are often revised or reinterpreted in ways that may significantly affect our business and our product candidates.

Foreign Regulation

In addition to regulations in the United States, we are subject to a variety of foreign regulations governing clinical trials of our product candidates and commercial sales and distribution of any products. Whether or not we or any collaborator of ours obtains FDA approval for a product candidate or product, we or the collaborator must obtain approval by the comparable regulatory authorities of foreign countries before we can commence clinical trials of the product candidate or marketing of the product in those countries. The approval process varies from country to country and the time may be longer or shorter than the time required for FDA approval. The requirements governing the conduct of clinical trials, product licensing, pricing and reimbursement vary greatly from country to country.

Under European Union regulatory systems, we may submit marketing authorization applications either under a centralized or a decentralized procedure. The centralized procedure, which is compulsory for medicines produced by certain biotechnological processes and optional for those which are highly innovative, provides for the grant of a single marketing authorization that is valid for all European Union member states. For drugs without approval in any member state, the decentralized procedure provides for approval by one or more other, or concerned, member states of an assessment of an application performed by one member state, known as the reference member state. Under this procedure, an applicant submits an application, or dossier, and related materials (including a draft summary of product characteristics, draft labeling and package leaflet) to the reference member state and concerned member states. The reference member state prepares a draft assessment and drafts of the related materials within 120 days after receipt of a valid application. Within 90 days of receiving the reference member state's assessment report, each concerned member state must decide whether to approve the assessment report and related materials. If a member state cannot approve the assessment report and related materials on the grounds of potential serious risk to public health, any disputed issues may eventually be referred to the European Commission, the decision of which would be binding on all member states.

Reimbursement

Sales of pharmaceutical products depend in significant part on the availability of third-party reimbursement. Third-party payors include government health administrative authorities, managed care providers, private health insurers and other organizations. These third-party payors are increasingly challenging the price and examining the cost-effectiveness of medical products and services, including prescription drugs. In addition, significant uncertainty exists as to the reimbursement status of newly approved prescription drugs and other healthcare products. We may need to conduct expensive pharmacoeconomic studies in order to demonstrate the cost-effectiveness of any of our products for which we or any collaborator of ours receives marketing approval. Our product candidates may not be considered cost-effective. It is time consuming and expensive for us or any collaborator of ours to seek reimbursement from third-party payors. Reimbursement may not be available or sufficient to allow the sale of any of our products for which we or any collaborator of ours receives marketing approval on a competitive and profitable basis.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003, or the MMA, imposes requirements for the distribution and pricing of prescription drugs for Medicare beneficiaries, and expands the prescription drug benefit under Medicare Part D. Under Part D, Medicare beneficiaries may enroll in prescription drug plans offered by private entities, which will provide coverage of outpatient prescription drugs. Part D plans include both stand-alone prescription drug benefit plans and prescription drug coverage as a supplement to Medicare Advantage plans. Unlike Medicare Part A and B, Part D coverage is not standardized. Part D prescription drug plan sponsors are not required to pay for all covered Part D drugs, and each drug plan can develop its own drug formulary that identifies which drugs it will cover and at what tier or level. However, Part D prescription drug formularies must include drugs within each therapeutic category and class of covered Part D drugs, although not necessarily all the drugs in each category or class. Any formulary used by a Part D prescription drug plan must be developed and reviewed by a pharmacy and therapeutic committee.

It is not clear what long-term effect the MMA will have on the prices paid for currently approved drugs and the pricing options for newly approved drugs. Government payment for some of the costs of prescription drugs may increase demand for any of our products for which we or any collaborator of ours receives marketing approval. However, any negotiated prices for our products covered by a Part D prescription drug plan will likely be lower than the prices we might otherwise obtain. Moreover, while the MMA applies only to drug benefits for Medicare beneficiaries, private payors often follow Medicare coverage policy and payment limitations in setting their own payment rates. Any reduction in payment that results from the MMA may result in a similar reduction in payments from non-governmental payors.

We expect that there will continue to be a number of federal and state proposals to implement governmental pricing controls and limit the growth of healthcare costs, including the cost of prescription drugs. Currently, Medicare is prohibited from negotiating directly with pharmaceutical companies for drugs. However, the U.S. Congress may consider legislation that would lift the ban on federal negotiations.

In some foreign countries, the proposed pricing for a drug must be approved before it may be lawfully marketed. The requirements governing drug pricing vary widely from country to country. For example, the European Union provides options for its member states to restrict the range of medicinal products for which their respective national health insurance systems provide reimbursement and to control the prices of medicinal products for human use. A member state may approve a specific price for the medicinal product or it may instead adopt a system of direct or indirect controls on the profitability of the company placing the medicinal product on the market. There can be no assurance that any country that has price controls or reimbursement limitations for pharmaceutical products will allow favorable reimbursement and pricing arrangements for any of our products for which we or any collaborator of ours receives marketing approval.

Employees

As of February 28, 2010, we had 116 employees, 43 of whom are Ph.D.s, M.D.s or both. Our management believes that relations with our employees are good. None of our employees is represented under a collective bargaining agreement.

Our Corporate Information

We were incorporated in Delaware in 1997 as a wholly owned subsidiary of R.J. Reynolds Tobacco Company. In August 2000, we became an independent company when we issued and sold stock to venture capital investors. Our principal executive offices are located at 200 East First Street, Suite 300, Winston-Salem, North Carolina 27101 and our telephone number is (336) 480-2100.

Our internet address is www.targacept.com. The information contained on, or that can be accessed through, our website is not incorporated by reference into this annual report. We have included our website address as a factual reference and do not intend it as an active link to our website. Our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and all amendments to those reports, are available to you free of charge through the Investor Relations page of our website as soon as reasonably practicable after such materials have been electronically filed with, or furnished to, the SEC.

Our trademarks include Targacept®, Pentad™, NNR Therapeutics™, TRIDMAC™ and Building Health, Restoring Independence™. Other service marks, trademarks and trade names appearing in this annual report are the properties of their respective owners.

Item 1A. Risk Factors.

Risks Related to Our Financial Results

We have a substantial accumulated deficit and may incur losses for the foreseeable future. We may never achieve profitability or, if we do achieve profitability, we may not sustain or grow it.

We were incorporated in 1997 and operated as a wholly owned subsidiary of R.J. Reynolds Tobacco Company until August 2000. We have a limited operating history. As of December 31, 2009, we had an accumulated deficit of $229.3 million. We had net loss of $39.4 million for the year ended December 31, 2009, net loss of $25.7 million for the year ended December 31, 2008 and net loss of $28.1 million for the year ended December 31, 2007. Our losses have historically resulted principally from costs incurred in connection with our research and development activities, including clinical trials, and from general and administrative expenses associated with our operations. We may incur losses for the foreseeable future as our clinical-stage and preclinical product candidates advance into later-stage development, as we progress our programs and invest in additional product opportunities and expand our research and development infrastructure. As a result, we will need to generate significant revenues to pay these expenses.

We derived a substantial portion of our revenue for 2009, 2008 and 2007 from our cognition-focused collaboration with AstraZeneca and our alliance with GlaxoSmithKline. We expect that a substantial portion of our operating cash flow in the next few years will depend on the following:

- whether and to what extent milestone events are achieved for TC-5214 under our December 2009 agreement with AstraZeneca and for AZD3480 or AZD1446 under our December 2005 agreement with AstraZeneca;
- whether and to what extent research and development-related milestone events are achieved under our agreement with GlaxoSmithKline;
- whether, following our completion of our ongoing Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia, AstraZeneca exercises its right to license TC-5619; and
- whether we establish additional strategic alliances, collaborations and licensing or other arrangements on terms favorable to us.

Sources that contributed to our revenue in 2009, 2008 and 2007 will not continue. In particular, the term of the preclinical research collaboration focused in cognition that we had been conducting with AstraZeneca under our December 2005 agreement expired in January 2010. We had received an aggregate of $26.5 million in research fees from AstraZeneca as of December 31, 2009, and research fee revenue generated from the preclinical research collaboration represented 21% of our net operating revenues for the year ended December 31, 2009, 45% of our net operating revenues for the year ended December 31, 2008 and 63% of our net operating revenues for the year ended December 31, 2007. In addition, we discontinued our product Inversine effective September 30, 2009 and do not currently have any source of product revenue.

If we or a collaborator of ours is unable to develop and commercialize one or more of our product candidates, if development is delayed or if revenue from sales of any product candidate that receives marketing approval is insufficient, we may not be profitable. Even if we are profitable for any particular period, we may not be able to sustain or grow our profitability on a quarterly or annual basis.

Our failure to obtain additional capital when needed could force us to delay, reduce or eliminate our product development programs or future commercialization efforts.

Successful drug development and commercialization requires significant amounts of capital. It is foreseeable that we will in the future require substantial additional capital in order to continue to conduct the research and development and clinical and regulatory activities necessary to bring our product candidates to market (or, where applicable for a particular product candidate, to the stage of development when a current or

potential future collaborator of ours may assume responsibility under the terms of the applicable agreement for funding further development and subsequent commercialization) and to establish sales and marketing capabilities. Our future capital requirements are difficult to forecast and will depend on many factors, including:

- the amount of revenue that we are able to generate, which we expect will depend substantially on the outcomes of the uncertainties described above under "*We have a substantial accumulated deficit and may incur losses for the foreseeable future. We may never achieve profitability or, if we do achieve profitability, we may not sustain or grow it.*";
- the progress of, and outcomes from, Phase 3 clinical development of TC-5214 and the amount and timing of development costs for TC-5214 payable by us;
- the scope, progress, duration, results and cost of clinical trials, as well as non-clinical studies and assessments, of our product candidates;
- the extent to which we retain development and commercialization rights or responsibilities for our product candidates that are not subject to our collaborations with AstraZeneca or our alliance with GlaxoSmithKline and incur associated development and manufacturing costs and costs to establish sales and marketing functions;
- the costs, timing and outcomes of regulatory reviews or other regulatory actions;
- the number and characteristics of product candidates that we pursue;
- the costs of preparing, filing and prosecuting patent applications and maintaining, enforcing and defending intellectual property-related claims;
- the costs of manufacturing-related services for our product candidates in clinical and late preclinical development;
- the rate of technological advancements for the indications that we target;
- the costs to satisfy our obligations under existing and potential future alliances and collaborations;
- the timing, receipt and amount of sales or royalties, if any, from our potential products; and
- the extent and scope of our general and administrative expenses.

In addition, we may seek additional capital due to market conditions or strategic considerations even if we believe we have sufficient funds for our current or future operating plans. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the ownership interests of our stockholders will be diluted and the terms may include liquidation or other preferences that materially and adversely affect the rights of our stockholders. Debt financing, if available, may involve agreements that include covenants limiting or restricting our ability to take specific actions such as incurring additional debt, making capital expenditures or declaring dividends. If we raise additional funds through alliance, collaboration or licensing arrangements with third parties, we may have to relinquish valuable rights to our technologies or product candidates or grant licenses on terms that are not favorable to us.

Our plans provide for us to continue, either alone, with AstraZeneca or GlaxoSmithKline or with one or more potential future collaborators, to advance our product candidates through the development process. We currently expect that our existing capital resources will enable us to fund our operations at least through the end of 2013. However, our operating plan may change as a result of many factors, including those described above, and we may need additional funds sooner than planned to meet operational needs and capital requirements for product development and commercialization. Our ability to raise funds if and when needed may be materially and adversely affected by deterioration that has been experienced in the U.S. and global financial markets and additional funds may not be available on terms that are acceptable to us, or at all. If adequate funds are not available on a timely basis, we may:

- terminate, delay or downsize clinical trials or manufacturing or other development activities for one or more of our product candidates;

- delay our establishment of sales and marketing capabilities or other activities that may be necessary to commercialize our product candidates; or
- curtail significant drug development programs that are designed to identify new product candidates.

Risks Related to the Development and Regulatory Approval of Our Product Candidates

Our success depends substantially on our most advanced product candidates, which are still under development. If we or a collaborator of ours is unable to bring one or more of these product candidates to market, or experience significant delays in doing so, our ability to generate product or royalty revenue and our likelihood of success will be harmed.

Our ability to generate product or royalty revenue over the next few years will depend substantially on the successful development and commercialization of our clinical-stage product candidates, including in particular: TC-5214 (for which we and AstraZeneca plan to conduct Phase 3 clinical development); AZD3480 (for which AstraZeneca plans to conduct additional Phase 2 clinical development in ADHD); AZD1446 (which AstraZeneca is currently evaluating in a clinical trial to assess safety and tolerability as an add-on to donepezil, which is the market leader in treatments for mild to moderate Alzheimer's disease, in subjects with Alzheimer's disease and in a Phase 2 clinical trial in adults with ADHD); TC-5619 (which we are currently evaluating in a Phase 2 clinical trial in cognitive dysfunction in schizophrenia); and TC-6987 (which is in Phase 1 clinical development).

Any of our product candidates could be unsuccessful if it:

- does not demonstrate acceptable safety and efficacy in preclinical studies or clinical trials or otherwise does not meet applicable regulatory standards for approval;
- does not offer therapeutic or other improvements over existing or future drugs used to treat the same condition;
- is not capable of being produced in commercial quantities at acceptable costs; or
- is not accepted in the medical community and by third-party payors.

We do not expect any of our current product candidates to be commercially available for at least the next several years, if at all. If we or any applicable collaborator of ours is unable to make our product candidates commercially available, we will not generate substantial product revenue and we will not be successful.

If the favorable results of either the completed Phase 2b clinical trial of TC-5214 as an adjunct therapy for major depressive disorder or the completed Phase 2 clinical trial of AZD3480 in adults with ADHD are not replicated in future clinical trials, we and AstraZeneca will not obtain the regulatory approvals required to market and sell the affected product candidate.

Favorable results in early clinical trials of a product candidate, such as our completed Phase 2b clinical trial of TC-5214 as an adjunct therapy for major depressive disorder and the completed Phase 2 clinical trial of AZD3480 in adults with ADHD, may not be replicated in later clinical trials that involve different numbers of subjects, different dosing regimens and durations, different subject populations and other differences in design or execution.

Our completed Phase 2b clinical trial of TC-5214 as an adjunct therapy for major depressive disorder was limited to subjects who did not respond adequately to the antidepressant citalopram. The planned Phase 3 development program for TC-5214 would include subjects who do not respond adequately to citalopram or any one of several other antidepressant therapies. It is possible that this difference in subject population, or any other difference in design between one or more of the planned Phase 3 clinical trials of TC-5214 and our completed Phase 2b clinical trial, will impact the likelihood that the favorable results achieved in the completed Phase 2b clinical trial will be replicated in Phase 3. Furthermore, our completed Phase 2b clinical trial was conducted

primarily in India and the planned Phase 3 development program would be conducted at investigative sites worldwide, including a significant number in the United States and Western Europe. Medical care in India is generally not as advanced as in the United States or Western Europe, and the treatment that subjects receive in a clinical trial in India may in some cases be their only medical treatment. As a result, clinical trial subjects in India may be less likely to discontinue participation from a clinical trial or to report adverse events experienced, either of which may impact the likelihood that the favorable results achieved in the completed Phase 2b clinical trial will be replicated. If the favorable results achieved in our completed Phase 2b clinical trial of TC-5214 are not replicated in future clinical trials, or if future clinical trials otherwise do not establish the safety and efficacy of TC-5214, we and AstraZeneca will not obtain the regulatory approvals required to market and sell TC-5214.

In addition, the completed Phase 2 clinical trial of AZD3480 in adults with ADHD was conducted at a single site with only 24 completed subjects and used a trial design in which subjects received each treatment (5mg AZD3480, 50mg AZD3480 and placebo) and in each case for only two weeks. Because subjects received each treatment, each subject served as his or her own control. Future clinical trials of AZD3480 in adults with ADHD are expected to be substantially larger trials, to be conducted at several sites and over a longer duration and to use placebo as a control such that each subject receives a particular dosing regimen of AZD3480 or placebo, but not both. It is possible that any of these differences or any other difference in trial design will impact the likelihood that the favorable results achieved in the completed Phase 2 clinical trial of AZD3480 in adults with ADHD will not be replicated in future clinical trials. If the favorable results achieved in the completed Phase 2 clinical trial of AZD3480 in adults with ADHD are not replicated, or if future clinical trials otherwise do not establish the safety and efficacy of AZD3480, we and AstraZeneca will not obtain the regulatory approvals required to market and sell AZD3480.

If the favorable results of the completed Phase 2 clinical trial of AZD3480 in adults with ADHD are not replicated in future clinical trials in children and adolescents, the commercial potential of AZD3480 would be materially and adversely affected.

The results of the completed Phase 2 clinical trial of AZD3480 in adults with ADHD may not be predictive of results that will be obtained in any future clinical trials of AZD3480 in children or adolescents with ADHD. A drug that has positive effects in adults may not necessarily have positive effects in younger patients. Children with ADHD tend to exhibit more hyperactivity than do adults with ADHD, and it is possible that this or any other difference in the characteristics of the disorder between adults and children will cause the results of the completed Phase 2 clinical trial adults with ADHD to be not predictive of results obtained in any future clinical trials of in children or adolescents with ADHD. In addition, to the extent ADHD in children and adolescents may functionally constitute a different indication than ADHD in adults, clinical trials of AZD3480 that have been completed in different indications have generated a range of efficacy results. In a Phase 2 clinical trial of AZD3480 that we conducted in Age Associated Memory Impairment, or AAMI, we achieved statistically significant results in favor of AZD3480 on the trial's three co-primary efficacy endpoints. In a Phase 2b trial of AZD3480 in mild to moderate Alzheimer's disease subsequently completed by AstraZeneca, known as the Sirocco trial, the results were inconclusive. Neither the active comparator used in the trial, donepezil, nor AZD3480 met the criteria for statistical significance on the primary outcome measure in the Sirocco trial. In a separate Phase 2b trial in cognitive dysfunction in schizophrenia of AZD3480 also completed by AstraZeneca in 2008, known as the HALO trial, AZD3480 did not meet the trial's criteria for statistical significance on the primary outcome measures.

Even if the favorable results in the completed Phase 2 clinical trial of AZD3480 in adults with ADHD are replicated in any future clinical trials of AZD3480 in adults with ADHD, if the results are not also replicated in any future clinical trials of AZD3480 in children or adolescents with ADHD, the FDA or other applicable regulatory authorities could limit the patient population for which AZD3480 is approved to adults. If the FDA or other applicable regulatory authorities limit the patient population for which AZD3480 to adults, the commercial potential of AZD3480 would be materially and adversely affected.

If we and AstraZeneca are unable to complete the Phase 3 development program for TC-5214 in time to submit an NDA to the FDA prior to October 1, 2012, or if other statutory conditions are not met, TC-5214 may not receive the five-year exclusivity period provided by applicable law and the ability of us and AstraZeneca to exclude third parties from marketing TC-5214 themselves would be substantially dependent on patents.

The Federal Food, Drug, and Cosmetic Act, or FDCA, provides a five-year period of marketing exclusivity in the United States to the first applicant to obtain approval of a new drug application, or NDA, for a drug that qualifies as a new chemical entity. During this exclusivity period, the FDA may not accept for review an abbreviated new drug application, or an ANDA, or another NDA for another version of the drug in question where the applicant does not own or have a legal right of reference to all the data required for approval (except that either of these applications may be submitted after four years with a certification that applicable patents are invalid or not infringed, in which case a timely challenge to the certification would trigger a stay of FDA's approval of the application for a defined term). The exclusivity period runs concurrently with any patents that cover the new chemical entity, but provides exclusivity independent from and irrespective of the patents. Accordingly, a new chemical entity approved in the United States has assurance of a statutory period of marketing exclusivity in the United States whether or not the patents that cover it are sufficiently strong to withstand challenge.

TC-5214 is one of two enantiomers of a racemate previously approved by the FDA. Enantiomers are mirror images of each other that have the same chemical but potentially different biological properties, and a racemate is a chemical mixture comprised of two corresponding enantiomers. Under Section 505(u) of the FDCA, as added by the FDA Amendments Act of 2007, an NDA applicant may, if certain conditions are met, elect that a single enantiomer of a previously approved racemate not be considered the same active ingredient as the racemate and thereby preserve potential eligibility for the single enantiomer as a new chemical entity. The election may only be made for an NDA submitted prior to October 1, 2012, when the statutory provision that permits the election is scheduled to expire unless re-authorized by the U.S. Congress. It is uncertain whether the statutory provision will be re-authorized. It is the goal of us and AstraZeneca to submit an NDA for TC-5214 in 2012. If we and AstraZeneca are unable to complete the Phase 3 development program for TC-5214 in time to submit an NDA for TC-5214 prior to October 1, 2012, whether because of delays in subject enrollment or for any other reason, or if other statutory conditions are not met, and the statutory provision is not reauthorized, TC-5214 will not receive the five-year exclusivity period and will be limited to three years of exclusivity provided by the FDCA for certain applications. In that case, we and AstraZeneca would be substantially reliant on patent protection to provide an extended term of exclusivity in the United States. Like any patent, the patents that we own or license covering TC-5214 and those that may issue in the future may be challenged, invalidated, rendered unenforceable or circumvented, any of which could limit our ability to stop third parties from marketing TC-5214 or related products themselves. If we and AstraZeneca are unable to enforce or defend patents that cover TC-5214 that we own or license and we cannot stop third parties from marketing TC-5214 or related products themselves, our commercialization of TC-5214 would be materially and adversely affected and our business would suffer.

If we or a collaborator of ours does not obtain the regulatory approvals required to market and sell our product candidates, our ability to generate product revenue will be materially impaired and our business will not be successful.

The preclinical laboratory testing, development, manufacturing and clinical trials of product candidates that we develop, whether independently or in collaboration with a third party, as well as their distribution, sale and marketing, are regulated by the FDA and other federal, state and local governmental and regulatory authorities in the United States and by similar agencies in other countries. We or a collaborator of ours must receive regulatory approval of each product candidate before we or the collaborator can market and sell it. We have only limited experience in pursuing regulatory approvals. Securing FDA approval requires the submission of extensive preclinical and clinical data and information about the chemistry and manufacture of, and control procedures for, each potential product. In addition, the supporting information submitted to the FDA must establish the safety and efficacy of the product candidate for each indicated use. The drug development and marketing approval

process takes many years, requires the expenditure of substantial resources, is subject to delays and can vary substantially based upon the type, complexity and novelty of the product candidates involved. In addition to the time and expense involved, the process is uncertain and neither we nor any applicable collaborator of ours may ever receive the required regulatory approvals. In addition, the FDA, the U.S. Congress or foreign governmental or regulatory authorities may from time to time change approval policies or adopt new laws or regulations that could prevent or delay our receipt of required approvals. Even if we or a collaborator of ours receives regulatory approval to market a particular product candidate, the approval will be subject to limitations on the indicated uses for which it may be marketed and may not permit labeling claims that are necessary or desirable for its promotion.

A Phase 1 clinical trial program typically takes several months to complete, a Phase 2 clinical trial program typically takes several months to two years to complete and a Phase 3 clinical trial program typically takes one to four years to complete. Moreover, Phase 3 clinical trials may not follow successful completion of Phase 2 clinical trials directly, as additional non-clinical assessments or clinical trials may first be required. Industry sources have reported that the preparation and submission of an NDA, which is required for regulatory approval in the United States, generally takes six months to one year to complete after completion of pivotal clinical trials. However, additional clinical trials may be required by the FDA or foreign regulatory authorities following completion of pivotal clinical trials and prior to seeking approval. The Pharmaceutical Research and Manufacturers of America has reported that only one out of five product candidates that enter clinical trials will ultimately be approved by the FDA for commercial sale.

The FDA may delay, limit or deny approval of any of our product candidates for many reasons. For example:

- clinical trial results may indicate that the product candidate is not safe or effective;
- the FDA may interpret our clinical trial results to indicate that the product candidate is not safe or effective, even if we or a collaborator of ours interprets the results differently; or
- the FDA may deem the processes and facilities that we, our collaborators or our third-party manufacturers propose to use in connection with the manufacture of the product candidate to be unacceptable.

If we or a collaborator of ours obtains the requisite regulatory approval for a particular product candidate, the approval may not extend to all indications for which approval was sought, which could limit the use of the product and materially and adversely impact our revenue.

Even if the FDA approves a product candidate for marketing and sale in the United States, applicable regulatory authorities in other countries may not approve the product candidate or may subject their approval to conditions such as additional product testing or otherwise cause delays. The regulatory approval process varies among countries, but generally includes all of the risks associated with obtaining FDA approval. In addition, many countries require a separate review process prior to marketing to determine whether their respective national health insurance schemes will pay for newly approved products, as well as the price that may be charged. This process will cause delays in the marketing of any of our product candidates that receives approval and could materially and adversely impact our revenue and results of operations.

If clinical trials for our product candidates are not successful, neither we nor any applicable collaborator of ours will obtain the regulatory approvals required to market and sell them.

To obtain the requisite regulatory approvals to market and sell any of our product candidates, we or any applicable collaborator of ours must demonstrate, through extensive preclinical studies and clinical trials, that the product candidate is safe and effective in humans. The number of clinical trials required to obtain approval varies depending on the particular product candidate, the disease or condition for which it is in development and the regulations applicable to it. Preclinical studies and clinical trials are lengthy and expensive, difficult to design

and implement and subject to a historically high rate of failure. The development of each of our product candidates involves significant risks at each stage of testing. A failure of one or more clinical trials of any of our product candidates could occur at any stage of testing. If we or any applicable collaborator of ours experiences failures in our ongoing or future clinical trials, or if we or the collaborator is not able to design clinical trials to establish the safety and efficacy of our product candidates and otherwise achieve the objectives of the trials, our product candidates may never be approved for sale or become commercially available.

We and any applicable collaborator of ours may not be able to obtain authority or approval from the FDA, other applicable regulatory authorities or the institutional review boards at our intended investigational sites to commence or complete our clinical trials. Before a clinical trial may commence in the United States, we or a collaborator of ours must submit an IND containing preclinical studies, chemistry, manufacturing, control and other information and a study protocol to the FDA. If the FDA does not object within 30 days after submission of the IND, then the trial may commence. If commenced, we or any applicable collaborator of ours, the FDA, other applicable regulatory authorities and institutional review boards may delay, suspend or terminate clinical trials of a product candidate at any time if, among other reasons, we or they believe the subjects participating in the clinical trials are being exposed to unacceptable health risks or for other reasons.

If we or any applicable collaborator of ours does not prove in clinical trials that our product candidates are safe and effective, neither we nor the collaborator will obtain marketing approvals from the FDA or other applicable regulatory authorities. In particular, one or more of our product candidates may not exhibit the expected medical benefits in humans, may cause harmful side effects or may have other unexpected characteristics that preclude regulatory approval for any or all indications of use or limit commercial use if approved.

Our research and preclinical programs and product candidates target diseases or disorders that are not well understood. For example, there is only limited scientific understanding of the causes of major depressive disorder, ADHD, Alzheimer’s disease and cognitive dysfunction in schizophrenia. In addition, there are no approved drugs that target NNRs to treat these diseases and disorders, and there is only limited scientific understanding of the relationships between these diseases and disorders and the neurological pathways targeted by our product candidates and research and preclinical programs. These uncertainties increase the risk that one or more of our clinical trials will not be successful.

If clinical trials for any of our product candidates are prolonged or delayed, we and any applicable collaborator of ours would experience a delay in the commercialization of the affected product candidates, which may require us to incur additional costs and delay our receipt of any revenue from potential product sales.

We cannot predict whether we or any applicable collaborator of ours will encounter problems with any completed, ongoing or planned clinical trials of our product candidates that will cause us, the collaborator or any regulatory authority to delay or suspend those clinical trials or delay the analysis of data derived from them. A number of events, including those described below, could delay the initiation or completion of any ongoing or planned clinical trial of any of our product candidates or otherwise negatively impact our ability to obtain regulatory approval for, and to market and sell, the product candidate:

- conditions imposed on us or any applicable collaborator of ours by the FDA or any foreign regulatory authority regarding the scope or design of the clinical trial;
- delays in recruiting and enrolling subjects into the clinical trial;
- delays in obtaining, or our inability to obtain, required approvals from institutional review boards, ethics committees or other reviewing entities at clinical sites selected for participation in the clinical trial;
- insufficient supply or deficient quality of the product candidates or other materials necessary to conduct the clinical trial;

- lower than anticipated retention rate of subjects in the clinical trial;
- negative or inconclusive results from the clinical trial, or results that are inconsistent with earlier results, that necessitate additional clinical study;
- serious and unexpected drug-related side effects experienced by subjects in the clinical trial; or
- failure of third-party contractors to us or any applicable collaborator of ours to comply with regulatory requirements or otherwise meet their contractual obligations to us or the collaborator in a timely manner.

Clinical trials require sufficient subject enrollment, which is a function of many factors, including the size of the patient population, the nature of the trial protocol, the proximity of subjects to clinical sites, the availability of effective treatments for the relevant disease and the eligibility criteria for the clinical trial. Delays in subject enrollment can result in increased costs and longer development times. The failure to enroll subjects in a clinical trial could delay the completion of the clinical trial beyond our current expectations. In addition, the FDA or foreign regulatory authorities could require us or any applicable collaborator of ours to conduct clinical trials for any of our product candidates with a larger number of subjects than we project. We or any applicable collaborator of ours may not be able to enroll a sufficient number of subjects in a timely or cost-effective manner. Furthermore, enrolled subjects may drop out of clinical trials, which could impair the validity or statistical analysis of those clinical trials.

We do not know whether any clinical trial of any of our product candidates will begin as planned, will need to be restructured or will be completed on schedule, if at all. Delays in clinical trials may result in increased development costs for our product candidates. In addition, if our clinical trials are delayed, our competitors may be able to bring products to market before we do and the commercial viability of our product candidates could be limited.

Regulatory authorities may require more data for any of our product candidates than we currently anticipate, which could cause us to incur additional costs, extend our development timelines or delay our receipt of any revenue from potential product sales.

The FDA or other applicable regulatory authorities may require more preclinical or clinical data for any of our product candidates or more time to evaluate that data than we currently anticipate because drugs that act on NNRs are not a well established class of drugs or because of experiences with drugs that act on NNRs that are developed or marketed by third parties. In particular, in February 2008, the FDA issued a public health advisory with regard to Pfizer's aid to smoking cessation product, Chantix. In July 2009, the FDA announced that it would require each of Chantix and Zyban, which is GlaxoSmithKline's aid to smoking cessation product, to include a boxed warning on its prescribing information. The warning makes more prominent the risk of serious mental health events, including changes in behavior, depressed mood, hostility, agitation and suicide-related events, that have been reported in some patients attempting to quit smoking while taking these drugs. The warning also states that the health benefits of quitting smoking are immediate and substantial and that the risks of the drug should be weighed against the benefits of use. Chantix acts on several NNR subtypes, as well as other molecular targets in the body. All of our product candidates currently in development affect the activity of one or more NNR subtypes. If the FDA or any foreign regulatory authority determines that any adverse medical experiences associated with Chantix have relevance to one or more of our product candidates, it may require us or any applicable collaborator of ours to generate more clinical data than we currently anticipate to establish the safety of the affected product candidate, which could increase the cost of the development program for the affected product candidate, extend the development timeline for the affected product candidate or delay our receipt of revenue from potential product sales of the affected product candidate.

Each of our product candidates will remain subject to ongoing regulatory review even if it receives marketing approval. If we or a collaborator of ours fails to comply with continuing regulations or if patients taking our products experience adverse health effects, we or any applicable collaborator could lose the approval or the sale of the affected products could be suspended or otherwise adversely affected.

Even if we or a collaborator of ours receives regulatory approval to market a particular product candidate, the approval could be conditioned on us or the collaborator conducting additional costly post-approval studies or could limit the indicated uses included in our labeling. Moreover, the product may later cause adverse medical experiences that limit or prevent its widespread use or commercial potential, force us or any applicable collaborator of ours to withdraw it from the market or impede or delay the ability of us or the collaborator to obtain regulatory approvals in additional countries. If any of our product candidates that becomes an approved product causes adverse medical experiences or becomes associated with any third party product that is associated with adverse medical experiences such as those described above under "*Regulatory authorities may require more data for any of our product candidates than we currently anticipate, which could cause us to incur additional costs, extend our development timelines or delay our receipt of any revenue from potential product sales.*" for Chantix, the overall commercial success of the affected product may be negatively impacted.

In addition, if any of our product candidates becomes an approved product, the manufacturer of the product and its facilities will continue to be subject to FDA review and periodic inspections to ensure adherence to applicable regulations. After receiving marketing approval, the manufacturing, labeling, packaging, adverse event reporting, storage, advertising, promotion and record keeping related to the product will remain subject to extensive regulatory requirements. We or any applicable collaborator of ours may be slow to adapt, or may never adapt, to changes in existing regulatory requirements or adoption of new regulatory requirements.

The Commissioner of the FDA, who was appointed in calendar year 2009, has put FDA-regulated entities on notice that they should expect to see more enforcement actions in all areas regulated by the FDA. Although we have not received any notice that we are the subject of any such enforcement action it is possible that we may be in the future and that could have a material adverse effect on our business. If we or any applicable collaborator of ours fails to comply with the requirements of the FDA and other applicable U.S. or foreign governmental or regulatory authorities or previously unknown problems with our products, manufacturers or manufacturing processes are discovered, we or the collaborator could be subject to administrative or judicially imposed sanctions, including:

- restrictions on the products, manufacturers or manufacturing processes;
- warning letters;
- civil or criminal penalties;
- fines;
- injunctions;
- product seizures or detentions;
- import bans;
- voluntary or mandatory product recalls and publicity requirements;
- suspension or withdrawal of regulatory approvals;
- total or partial suspension of production; and
- refusal to approve pending applications for marketing approval of new drugs or supplements to approved applications.

Because we have multiple compounds and are considering a variety of target indications, we may expend our limited resources to pursue a particular product candidate or indication and fail to capitalize on product candidates or indications that may be more profitable or for which there is a greater likelihood of success.

Because we have limited financial and managerial resources, we must focus on research programs and product candidates for the specific indications that we believe are the most promising. As a result, we may forego or delay pursuit of opportunities with other product candidates or other indications that later prove to have greater commercial potential. Our resource allocation decisions may cause us to fail to capitalize on viable commercial products or profitable market opportunities. Furthermore, if we do not accurately evaluate the commercial potential or target market for a particular product candidate, we may relinquish valuable rights to that product candidate through collaboration, licensing or other royalty arrangements in cases in which it would have been advantageous for us to retain sole development and commercialization rights.

If we do not achieve specified discovery and development events in our alliance with GlaxoSmithKline for which we would be entitled to receive milestone payments, our research and development activities in the alliance may not be self-funding and we may need to utilize other financial resources to conduct the activities, which could materially and adversely affect our ability to advance the development of our other product candidates.

We have an ongoing alliance with GlaxoSmithKline that is designed to discover, develop and market product candidates that selectively target specified NNR subtypes in specified therapeutic focus areas. Under the alliance agreement, we have agreed, at our sole expense, to seek to discover product candidates that target specified NNR subtypes for each therapeutic focus area of the alliance and to develop the most promising product candidate for each therapeutic focus area through a Phase 2 clinical proof of concept trial. We are eligible to receive contingent milestone payments from GlaxoSmithKline as we advance product candidates in each therapeutic focus area through preclinical and Phase 1 clinical development. If we do not achieve specified milestone events, we will not receive payments sufficient to fund our research and development obligations in the alliance or otherwise to realize the expected benefit from the alliance. If that occurs, we may have to allocate available financial resources to our obligations in the alliance in lieu of employing those resources to advance the development of our product candidates outside of the alliance that may ultimately prove to have greater commercial potential.

We may not be successful in our efforts to identify or discover additional product candidates.

A key element of our strategy is to develop and commercialize drugs that selectively target specific NNR subtypes. We seek to do so through our understanding of the role of specific NNRs in the nervous system, our scientific expertise and the use of Pentad.

A significant portion of the research that we are conducting involves new and unproven compounds. Research programs to identify new product candidates require substantial technical, financial and human resources. These research programs may initially show promise in identifying potential product candidates, yet fail to yield product candidates for clinical development for a number of reasons, including:

- the research methodology used may not be successful in identifying potential product candidates; or
- potential product candidates may, on further study, be shown to have harmful side effects or other characteristics that indicate that they are unlikely to be effective products.

If we are unable to develop suitable product candidates through internal research programs, we will not be able to overcome attrition in drug development and generate revenue in future periods, which could result in significant harm to our financial position and materially and adversely impact our stock price. Any additional product candidates that we are able to develop through our internal research programs will require the commitment of substantial time and financial resources for further preclinical research and clinical development.

Risks Related to Our Dependence on Third Parties

The successful development and commercialization of TC-5214 depends substantially on our December 2009 collaboration with AstraZeneca.

We entered into our collaboration agreement with AstraZeneca for TC-5214 in December 2009. We cannot predict the ultimate success of the collaboration. The collaboration involves a complex allocation of rights and responsibilities, provides for milestone payments to us if specified development, regulatory and first commercial sale milestone events are achieved and provides us with royalty-based revenue if TC-5214 is successfully commercialized. We and AstraZeneca have agreed on an initial development program for TC-5214 for major depressive disorder, but AstraZeneca has the authority to make changes to the initial major depressive disorder program and also has decision-making authority for many other matters in our collaboration. In addition, AstraZeneca has the right to assume control of patent matters with respect to TC-5214.

AstraZeneca is responsible for the conduct of substantially all future development of TC-5214, except for non-clinical studies ongoing at the time of our agreement, and has significant control over the conduct and timing of development efforts with respect to TC-5214. We have little control over the amount and timing of resources that AstraZeneca devotes to the development of TC-5214. If AstraZeneca fails to devote sufficient financial and other resources, the development and potential commercialization of TC-5214 would be delayed. This would result in a delay in milestone payments and, if regulatory approval to market and sell TC-5214 is obtained, royalties that we could receive on product sales.

AstraZeneca has the right to terminate our agreement in its entirety:

- within a specified period following completion of the Phase 3 development program for TC-5214 as an adjunct therapy;
- if AstraZeneca determines there to be a serious safety issue regarding the continued development or commercialization of TC-5214;
- if, having obtained the advice of independent patent counsel, AstraZeneca believes that the commercialization of TC-5214 is more likely than not to infringe or misappropriate intellectual property rights of third parties in the United States or any two specified major pharmaceutical markets and is unable to obtain a license on commercially reasonable terms; or
- for an uncured material breach by us.

In addition, AstraZeneca can terminate our agreement on a major pharmaceutical market by major pharmaceutical market basis at any time beginning four years after effectiveness of our agreement, except that, if AstraZeneca terminates our agreement with respect to the United States, our agreement will terminate in its entirety.

If AstraZeneca terminates our agreement at any time, for any reason, it would negatively impact our development of TC-5214 and materially harm our business and could accelerate our need for additional capital. In particular, we would have to fund any further clinical development and commercialization of TC-5214 on our own, seek another collaborator or licensee for clinical development and commercialization or abandon the development and commercialization of TC-5214.

If TC-5214 exhibits a similar overall therapeutic profile to AstraZeneca's product Seroquel XR, AstraZeneca may de-emphasize the development or commercialization of TC-5214, which would materially and adversely affect the revenue that we derive based on TC-5214.

AstraZeneca's product Seroquel XR is approved by the FDA for use, among other things, as an adjunct to antidepressant therapy for major depressive disorder. TC-5214 is in development as an adjunct to antidepressant therapy and as a monotherapy for major depressive disorder. Until the Phase 3 development program for

TC-5214 is completed and regulatory approval is obtained, the overall therapeutic profile of TC-5214 and any patient population for which TC-5214 may be considered safe and effective are uncertain. AstraZeneca has control or significant influence over the conduct of future development and regulatory approval activities for TC-5214. If one or more Phase 3 clinical trials of TC-5214 indicate that its overall therapeutic profile may be similar to the overall therapeutic profile of Seroquel XR, AstraZeneca may de-emphasize or otherwise fail to devote sufficient financial and other resources to the development of TC-5214. In that event, the development and potential commercialization of TC-5214 would be delayed. This would result in a delay of milestone payments and, if regulatory approval to market and sell TC-5214 is obtained, royalties on product sales that we could receive and could result in us not receiving milestone payments or royalties at all. Even if TC-5214 is successfully developed and regulatory approvals are obtained, if AstraZeneca de-emphasizes or otherwise fails to devote sufficient financial and other resources to the commercialization of TC-5214 for any reason, royalties that we could receive on product sales would be materially and adversely affected.

The successful development and commercialization of AZD3480 and AZD1446 depends substantially on our December 2005 collaboration with AstraZeneca.

We entered into our collaboration agreement with AstraZeneca focused on cognitive disorders in December 2005. The collaboration involves a complex allocation of rights, provides for milestone payments to us based on the achievement of specified development, regulatory and first commercial sale milestone events and provides us with royalty-based revenue if AZD3480, AZD1446 or another product candidate subject to the collaboration is successfully commercialized. AstraZeneca has decision-making authority for most matters in our collaboration, including, as long as it meets its diligence obligations under the agreement, whether to proceed with further development and potential commercialization of any particular product candidate in the collaboration and, if so, for what indication(s). In addition, AstraZeneca has the right to assume control of patent matters with respect to AZD3480 and AZD1446 and has exercised its right with respect to the prosecution of some of our applicable patents.

AstraZeneca is generally responsible for conducting and funding substantially all future development of AZD3480 and AZD1446. As a result, AstraZeneca has significant control over the conduct and timing of development efforts with respect to AZD3480 and AZD1446. We have little control over the amount and timing of resources that AstraZeneca devotes to the development of AZD3480 or AZD1446. If AstraZeneca fails to devote sufficient financial and other resources to the development of either or both of AZD3480 and AZD1446, the development and potential commercialization of the affected product candidate(s) would be delayed. This would result in a delay in milestone payments and, if regulatory approval to market and sell AZD3480 or AZD1446 is obtained, royalties that we could receive on product sales.

In addition, if at any time AstraZeneca determines not to conduct further development of AZD3480 or AZD1446 and the determination does not result in a failure to meet its diligence obligations under the agreement, we would not be permitted to conduct development of the affected product candidate(s) independently or with another collaborator and would not benefit from any commercial potential of the affected product candidate(s).

AstraZeneca has the right to terminate our agreement in its entirety upon 90 days notice. If AstraZeneca terminates our agreement at any time, for any reason, it would negatively impact the development of AZD3480 and AZD1446 and materially harm our business and could accelerate our need for additional capital. In particular, we would have to fund any further clinical development and commercialization of AZD3480 and AZD1446 on our own, seek another collaborator or licensee for clinical development and commercialization or abandon the development and commercialization of AZD3480 and AZD1446.

If AstraZeneca were to exercise its future right to license TC-5619 but fail to devote sufficient financial and other resources to its development, our ability to derive revenue based on TC-5619 would be materially and adversely affected.

If AstraZeneca licenses TC-5619 following our completion of our ongoing Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia, AstraZeneca would become generally responsible for conducting and funding substantially all future development and regulatory approval activities for TC-5619 and have significant control over the conduct and timing of development efforts with respect to TC-5619. If AstraZeneca were to fail to devote sufficient financial and other resources to the development of TC-5619, whether in favor of an internal product candidate or for any other reason, the development and potential commercialization of TC-5619 would be delayed. This would result in a delay in milestone payments and, if regulatory approval to market and sell TC-5619 is obtained, royalties that we could receive on product sales.

If GlaxoSmithKline exercises any of the exclusive options that may be triggered under our alliance agreement, the successful development and commercialization of the licensed product candidates will depend substantially on GlaxoSmithKline.

We entered into our agreement with GlaxoSmithKline in July 2007. Prior to entering into the agreement, we did not have a history of working together with GlaxoSmithKline and we cannot predict the ultimate success of the alliance. Under the agreement, if we achieve clinical proof of concept for a lead product candidate for any of the therapeutic focus areas of the alliance, GlaxoSmithKline would have an exclusive option for an exclusive license to the lead product candidate and up to two other product candidates in development in the alliance for the same therapeutic focus area on a worldwide basis. If GlaxoSmithKline were to exercise its option and pay the applicable exercise fee, GlaxoSmithKline would become responsible for using diligent efforts to conduct later-stage development and commercialization of the lead product candidate at its sole expense. In that event, we would have limited control over the amount and timing of resources that GlaxoSmithKline dedicates to the development of our licensed product candidates. If GlaxoSmithKline were to fail to devote sufficient financial and other resources to the development of our licensed product candidates, whether in favor of internal product candidates or for any other reason, the development and potential commercialization of our licensed product candidates would be delayed. This would result in a delay in milestone payments and, if regulatory approval to market and sell a licensed product candidate is obtained, royalties that we could receive on product sales. Our ability to generate further revenue from the alliance would depend on GlaxoSmithKline's efforts and abilities to establish the safety and efficacy of our product candidates, to obtain regulatory approvals and to achieve market acceptance.

If the shift in research focus away from certain neuroscience areas announced by GlaxoSmithKline in February 2010 leads to the discontinuation of one or more of the therapeutic focus areas of our alliance, or diminished interest in licensing product candidates advanced in one or more programs in the therapeutic focus areas of our alliance, we will not realize the expected benefits of the alliance for those programs.

In February 2010, GlaxoSmithKline announced plans to cease discovery research in selected neuroscience areas, specifically including pain, which is one of the therapeutic focus areas of our alliance with GlaxoSmithKline. Discussions with GlaxoSmithKline regarding the effects of its strategic change on our alliance are ongoing. Until these discussions are completed, we cannot be certain of the overall impact, but we currently anticipate that multiple therapeutic focus areas in the alliance will be discontinued. In that event, we would no longer be eligible to receive contingent milestone payments from GlaxoSmithKline as we advance product candidates in the programs for the applicable therapeutic focus areas through preclinical and Phase 1 clinical development. If we were to desire to continue any of these programs, we would need to find another collaborator or fund the program ourselves. If we were unable to find another collaborator, we could have to terminate, suspend or delay, or otherwise limit the financial or other resources we devote to, the applicable programs. Even if a particular therapeutic focus area were not to be discontinued in the alliance, GlaxoSmithKline could seek to establish a threshold for a determination of Phase 2 clinical proof of concept in the therapeutic focus area that is difficult to achieve, which could lead to protracted discussions and potential disagreements that would delay the

progress of the applicable program and reduce the likelihood that GlaxoSmithKline will have and exercise its option in the therapeutic focus area, that we would receive the option exercise fee or any of the downstream payments called for by our alliance agreement with respect to the therapeutic focus area and that we would benefit from GlaxoSmithKline's expertise in the therapeutic focus area and substantial resources.

We will depend on alliances and collaborations with third parties for the development and commercialization of some of our product candidates. If our alliances and collaborations are not successful, we may not be able to capitalize on the market potential of these product candidates.

In addition to our collaborations with AstraZeneca and our alliance with GlaxoSmithKline, we intend to selectively enter into alliances and collaborations for target indications for which our potential collaborator has particular expertise or that represent large primary care markets that must be served by large sales and marketing organizations. Our ability to generate revenue from our alliances and collaborations will depend on our collaborators' abilities to establish the safety and efficacy of our product candidates, to obtain regulatory approvals and to achieve market acceptance. Strategic alliances and collaborations involving our product candidates, including our collaborations with AstraZeneca and our alliance with GlaxoSmithKline, pose many risks to us, including:

- collaborators have significant discretion in determining the amount and timing of efforts and resources that they will apply to these alliances and collaborations or to the development of our licensed product candidates;
- collaborators may interpret clinical trial or non-clinical study results differently than we do, may pursue further development and commercialization of our product candidates for indications that we do not believe are optimal, may not pursue further development and commercialization of our product candidates at all or may elect not to continue or renew research and development programs based on preclinical or clinical trial results, changes in their strategic focus or available funding, or external factors such as an acquisition that diverts resources or creates competing priorities;
- collaborators may delay clinical trials, provide insufficient funding for a clinical trial program, stop a clinical trial or abandon a product candidate, repeat or conduct new clinical trials or require a new formulation of a product candidate for clinical testing;
- collaborators could independently develop, or develop with third parties, products that compete directly or indirectly with our products or product candidates if the collaborators believe that competitive products are more likely to be successfully developed or can be commercialized under terms that are more economically attractive;
- collaborators with marketing and distribution rights to one or more products may not commit enough resources to their marketing and distribution;
- collaborators may not properly maintain or defend our intellectual property rights or may use our proprietary information in such a way as to invite litigation that could jeopardize or invalidate our proprietary information or expose us to potential litigation;
- disputes may arise between us and collaborators that result in the delay or termination of the research, development or commercialization of our product candidates, that result in costly litigation or arbitration that diverts management attention and resources or that, if resolved unfavorably to us, result in adverse financial consequences for us under the terms of the applicable agreements; and
- alliances and collaborations may be terminated and, if terminated, may result in a need for additional capital to pursue further development of the applicable product candidates.

Alliances and collaborations may not lead to development of product candidates or commercialization of products in the most efficient manner or at all.

In addition, there have been a significant number of recent business combinations among large pharmaceutical companies that have resulted in a reduced number of potential future collaborators. If a present or future collaborator of ours were to be involved in a business combination, the continued pursuit and emphasis on our product development program could be delayed, diminished or terminated.

Our ability to establish additional alliances and collaborations may be limited by the terms of our agreements with AstraZeneca and GlaxoSmithKline. If we do not establish additional alliances and collaborations, we may have to alter our development plans.

Our drug development programs and potential commercialization of our product candidates will require substantial additional cash to fund expenses. Our strategy includes selectively seeking alliances and collaborations to assist us in furthering development and potential commercialization of some of our product candidates. We intend to do so especially for target indications for which our potential collaborator has particular expertise or that involve large primary care markets that must be served by large sales and marketing organizations.

Under the terms of our 2005 agreement with AstraZeneca, we have the right to offer to AstraZeneca the right to license any compound that meets pre-defined criteria for any NNR other than the a4ß2 NNR that we may in the future seek to exploit for any condition characterized by cognitive impairment for which AstraZeneca has development and commercialization rights under our agreement. We made such an offer with respect to TC-5619, which following a process under our agreement led to AstraZeneca's future right to license TC-5619. However, if we do not offer a compound that meets pre-defined criteria for any NNR other than the a4ß2 NNR to AstraZeneca, we are generally not permitted to develop or commercialize the compound for any of these indications. Similarly, under the terms of our 2009 agreement with AstraZeneca, for three years from the date the collaboration agreement became effective, we are not permitted to conduct a Phase 2 or later clinical trial, or to commercialize, a compound as an adjunct therapy for major depressive disorder. As a result, our ability to seek additional alliances and collaborations for the target indications for our two collaborations with AstraZeneca is substantially limited. In addition, AstraZeneca may under certain circumstances have a right of first negotiation under our 2005 agreement with AstraZeneca for the development and commercialization of compounds that act by binding to NNRs for depression, anxiety and bipolar disorder.

We have also agreed in our alliance agreement with GlaxoSmithKline that, for so long as we are required to conduct research activities in a particular therapeutic focus area of the alliance, or for so long as there are any product candidates in development or being commercialized in the alliance in that therapeutic focus area, we will work in the therapeutic focus area exclusively with GlaxoSmithKline with respect to product candidates with activity in the therapeutic focus area derived from binding to NNRs. As a result, our ability to seek additional alliances for any of these areas is substantially limited during the term of our alliance with GlaxoSmithKline. The therapeutic focus areas of our alliance with GlaxoSmithKline currently are pain, smoking cessation, addiction, obesity and Parkinson's disease.

We face significant competition in seeking appropriate alliances and collaborations. Alliances and collaborations are complex and time-consuming to negotiate and document. We may not be able to negotiate them on acceptable terms, or at all. If we cannot, we may have to curtail the development of a particular product candidate, reduce or delay its development program or one or more of our other development programs, delay its potential commercialization or reduce the scope of any sales or marketing activities, or increase our expenditures and undertake development or commercialization activities at our own expense. If we elect to increase our expenditures to fund development or commercialization activities on our own, we may need to obtain additional capital, which may not be available to us on acceptable terms or at all. If we do not have sufficient funds, we will not be able to bring our product candidates to market and generate product revenue.

If AstraZeneca's contract manufacturer for TC-5214 fails to devote sufficient resources to TC-5214, or if its performance is substandard, clinical trials and product introductions of TC-5214 may be delayed or there may be a shortage of supply.

Under the terms of our 2009 agreement with AstraZeneca, AstraZeneca is responsible for the manufacture and supply of TC-5214 and has assumed our rights and obligations under our applicable agreements with third parties, including a supply agreement with Poli Industria Chimica, S.P.A., or Poli, and Interchem Corporation, or Interchem, for the pharmaceutical development and supply of the active ingredient form of TC-5214. The agreement with Poli and Interchem assumed by AstraZeneca provides for it to purchase its requirements for the active ingredient form of TC-5214 exclusively from Poli through Interchem during the term of the agreement, subject to specified conditions. Because of the exclusive supply relationship, if Poli breaches or fails to perform as agreed under the agreement, or if the agreement terminates for any reason, there may be a delay or interruption in manufacturing of TC-5214 that leads to a shortage of supply. If AstraZeneca were to have the right to change the manufacturer for the active ingredient form of TC-5214 and were to make the change for any reason, in addition to the risks associated with changing a contract manufacturer described below under "*If our contract manufacturers fail to devote sufficient resources to our concerns, or if their performance is substandard, our clinical trials and product introductions may be delayed or there may be a shortage of commercial supply.*," it would be dependent on Poli to effect or facilitate a successful transfer of the manufacturing technology for TC-5214 to AstraZeneca or a replacement contract manufacturer. Such a technology transfer would require review and approval by the FDA or foreign regulatory authorities and would also likely require an inspection of the new manufacturer to assess cGMP compliance, both of which would be time-consuming and increase the likelihood of a delay or interruption in manufacture or a shortage of supply of TC-5214. Any delay or interruption in manufacture or shortage of supply of TC-5214 could delay or prevent the initiation or completion of clinical trials of TC-5214, the submission of applications for regulatory approvals of TC-5214 or the receipt of regulatory approvals for TC-5214, materially and adversely affect the commercialization of TC-5214 or result in higher costs or lost product revenue.

If our contract manufacturers fail to devote sufficient resources to our concerns, or if their performance is substandard, our clinical trials and product introductions may be delayed or there may be a shortage of commercial supply.

Our product candidates require precise, high quality manufacturing. We have limited internal manufacturing capability. We have historically manufactured our product candidates only in small quantities for preclinical testing and have contracted with third parties to manufacture, in collaboration with us, our product candidates for clinical trials. If any of our product candidates is approved by the FDA or by foreign regulatory authorities for marketing and sale, it will need to be manufactured in substantially larger, commercial quantities. Our experience in the manufacture of drugs in commercial quantities is limited to our contractual arrangements with third parties to manufacture our now discontinued product Inversine and its active ingredient.

We currently rely on single third-party contract manufacturers for each of our product candidates and we intend to continue to rely on third-party manufacturers to supply, store and distribute our product candidates for our clinical trials and to manufacture commercial supplies of any product candidate that is approved for sale. Our reliance on third-party manufacturers will expose us to risks that could delay or prevent the initiation or completion of our clinical trials, the submission of applications for regulatory approvals, the receipt of regulatory approvals or the commercialization of our products or result in higher costs or lost product revenue. In particular, any contract manufacturer:

- could encounter difficulties in achieving volume production, quality control and quality assurance and suffer shortages of qualified personnel, which could result in its inability to manufacture sufficient quantities to meet our clinical timelines or to commercialize our product candidate;
- could terminate or not renew its manufacturing agreement with us, based on its own business priorities, at a time that is costly or inconvenient for us;

- could fail to establish and follow current good manufacturing practices, or cGMP, mandated by the FDA or foreign regulatory authorities and required for approval of our product candidates or fail to document its adherence to cGMP, either of which could lead to significant delays in the availability of material for clinical study and delay or prevent filing or approval of marketing applications for our product candidates; and
- could breach, or fail to perform as agreed under, its manufacturing agreement with us.

We expect to rely initially on a single contract manufacturer for any product candidate that we successfully bring to market. Changing any manufacturer that we engage for a particular product or product candidate may be difficult, as the number of potential manufacturers is limited and we will have to compete with third parties for access to those manufacturing facilities. cGMP manufacturing processes and procedures typically must be reviewed and approved by the FDA or foreign regulatory authorities and changing manufacturers may require re-validation of any new facility for cGMP compliance, which would likely be costly and time-consuming. We may not be able to engage replacement manufacturers on acceptable terms quickly or at all. In addition, our contract manufacturers located in foreign countries may be subject to import limitations or bans. As a result, if any of our contract manufacturers is unable, for whatever reason, to supply the contracted amounts of any product that we successfully bring to market, a shortage would result which would have a negative impact on our revenue.

Drug manufacturers are subject to ongoing periodic unannounced inspection by the FDA, the U.S. Drug Enforcement Agency and corresponding state and foreign agencies to ensure strict compliance with cGMP, other government regulations and corresponding foreign standards. While we are obligated to audit the performance of third-party contractors, we do not have control over our third-party manufacturers' compliance with these regulations and standards. Failure by our third-party manufacturers or us to comply with applicable regulations could result in sanctions being imposed on us, including fines, injunctions, civil penalties, failure of the government to grant pre-market approval of drugs, delays, suspension or withdrawal of approvals, seizures or recalls of product, operating restrictions and criminal prosecutions.

If third parties on which we rely for clinical trials do not perform as contractually required or as we expect, we may not be able to obtain regulatory approval for or commercialize our product candidates.

We do not have the ability to independently conduct the clinical trials required to obtain regulatory approval for our product candidates. We and applicable collaborators for our product candidates depend on independent clinical investigators and, in some cases, contract research organizations and other third-party service providers to conduct the clinical trials of our product candidates and expect to continue to do so. We rely heavily on these parties for successful execution of our clinical trials, but we do not control many aspects of their activities. Nonetheless, we are responsible for confirming that each of our clinical trials is conducted in accordance with its general investigational plan and protocol. Moreover, the FDA and foreign regulatory authorities require us to comply with regulations and guidelines, commonly referred to as good clinical practice, for conducting and recording and reporting the results of clinical trials to assure that data and reported results are credible and accurate and that the trial participants are adequately protected. Our reliance on third parties that we do not control does not relieve us of these responsibilities and requirements.

Third parties may not complete activities on schedule or may not conduct our clinical trials in accordance with regulatory requirements or the respective trial plans and protocols. These risks may be heightened for clinical trials that we conduct outside of North America and Western Europe. In particular, most of the clinical trial sites planned to be included in our ongoing Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia are located in India. Language barriers and the limited experience of some clinical investigators in India in conducting clinical trials in accordance with standards set forth by the FDA and applicable regulatory authorities in India may increase the risk of non-compliance. The failure of third parties to carry out their obligations could impair the credibility or reliability of the data generated in clinical trials of our product

candidates, require a trial to be repeated and increase the overall cost of a development program, delay or prevent the development, approval and commercialization of our product candidates or result in enforcement action against us.

If unfavorable market conditions adversely affect the ability of third parties to carry out their obligations to us or our collaborators, the development of our product candidates may be delayed.

Unfavorable conditions that have been experienced in recent years in the global credit and financial markets may adversely affect the ability of third parties with which we or a collaborator of ours contract for services related to clinical trials or manufacturing of any of our product candidates to carry out their obligations. The unfavorable market conditions may cause any of these third parties to be unable to obtain financing for its operations or not to sufficiently staff or otherwise resource its obligations to us or a collaborator of ours. A significant interruption in the performance of these third parties may result in delays in the conduct or completion of clinical trials for our product candidates. A delay in the conduct or completion of clinical trials for any of our product candidates may extend the overall development timeline or increase the development costs for the product candidate, delay our receipt of revenue from potential sales of the product candidate or have an adverse effect on our ability to establish a strategic alliance, collaboration or licensing or other arrangement with respect to the product candidate on terms favorable to us.

Risks Related to Our Intellectual Property

If we are unable to protect our intellectual property effectively, our competitors may develop and market similar products and the value of our technology and our ability to compete would be damaged.

Our continued success depends significantly on the ability of us or any applicable collaborator of ours to obtain and maintain meaningful intellectual property protection for our product candidates, technology and know-how. We generally seek to protect our compounds and technologies by, among other methods, filing U.S. and foreign patent applications related to our proprietary technology that is important to the development of our business. We file patent applications directed to our product candidates in an effort to establish intellectual property positions regarding new chemical entities and uses in the treatment of diseases and disorders.

The patent positions of companies like ours are generally uncertain and involve complex legal and factual questions. Our ability to maintain and solidify our proprietary position for our product candidates and technology will depend on the success that we or any applicable collaborator of ours has in obtaining effective patent claims and enforcing claims that are granted. We do not know whether any of our patent applications or those patent applications that we license will result in the issuance of any patents. Our issued patents and those that may issue in the future, or those licensed to us, may be challenged, invalidated, rendered unenforceable or circumvented, any of which could limit our ability to stop competitors from marketing related products. Moreover, the U.S. Supreme Court's 2007 decision in *KSR International Co. vs. Teleflex, Inc.* may in some cases make it more difficult to obtain a patent, or to withstand a validity challenge to any issued patent, for pharmaceutical products that have a relationship to other pharmaceutical products, such as single enantiomers like TC-5214, combination products or specific salt forms. In addition, the rights granted under any issued patents may not provide us with competitive advantages against competitors with similar compounds or technologies. Furthermore, our competitors may independently develop similar technologies in a manner that does not infringe our patents or other intellectual property. If we are unable to obtain, enforce or defend the patents with respect to our product candidates, our ability to commercialize our product candidates would be materially and adversely affected and our business would suffer.

Although we own or otherwise have rights to a number of patents, these patents may not effectively exclude competitors from engaging in activities that compete with us. Furthermore, the issuance of a patent is not conclusive as to its validity or enforceability, and third parties may challenge the validity or enforceability of our

patents. Because patent applications in the United States and many foreign countries are confidential for a period of time after filing, and because publications of discoveries in the scientific literature often lag behind actual discoveries, we cannot be certain that we were the first to invent the inventions claimed in our issued U.S. patents or pending patent applications, or that we were the first to file for protection of the inventions set forth in the foreign patents or patent applications. It is possible that a competitor may successfully challenge our patents or that challenges will result in the elimination or narrowing of patent claims and, therefore, reduce our patent protection.

Because of the extensive time required for development, testing and regulatory review of a new drug, it is possible that any patent covering one of our product candidates may expire before the product candidate can be commercialized or remain in force for only a short period following initial commercialization. In either case, any advantages of the patent would be limited. The patent laws of various foreign countries in which we intend to compete may not protect our intellectual property to the same extent as the laws of the United States. Changes either in patent laws or in interpretations or enforcement of patent laws in the United States and other countries may diminish the value of our intellectual property or narrow the scope of our patent protection.

If we are unable to protect the confidentiality of our proprietary information and know-how, the commercial value of our technology and product candidates could be reduced.

In addition to patents, we rely on protection of trade secrets, know-how and confidential and proprietary information to maintain our competitive position. For example, we generally do not seek patent protection for the computer-based molecular design technologies that form part of Pentad and instead seek to maintain those technologies as trade secrets.

To maintain the confidentiality of trade secrets and proprietary information, we generally enter into confidentiality agreements with our employees, consultants, contractors and collaborators upon the commencement of our relationship with them. These agreements typically require that all confidential information developed by the individual or made known to the individual by us during the course of the individual's relationship with us be kept confidential and not disclosed to third parties. However, we may not obtain these agreements in all circumstances, and individuals with whom we have these agreements may not comply with their terms. Even if obtained, these agreements may not provide meaningful protection for our trade secrets or other proprietary information or an adequate remedy in the event of their unauthorized use or disclosure. The loss or exposure of our trade secrets or other proprietary information could impair our competitive position.

We also typically enter into agreements with employees that provide that inventions conceived by them in the course of rendering services to us are our exclusive property and, where appropriate, we enter into similar agreements with consultants and contractors. To the extent that our employees, consultants or contractors use technology or know-how owned by others in their work for us, disputes may arise as to the rights in related inventions.

If we fail to comply with our obligations in our intellectual property licenses with third parties, we could lose license rights that are important to our business and, if we have sublicensed our license rights to a third party, the loss of the license rights may breach our obligations to our sublicensee.

We are a party to various license agreements. In particular, we license patent rights covering the pharmaceutical composition and methods of use of TC-5214 from University of South Florida Research Foundation and Yale University and have sublicensed these patent rights to AstraZeneca. We may enter into additional licenses in the future. Our existing licenses impose, and we expect future licenses will impose, various diligence, milestone payment, royalty, insurance and other obligations on us. If we fail to comply with these obligations, whether as a result of actions or inactions by AstraZeneca or any other present or future collaborator of ours to which we out-license patents rights that we have in-licensed from a third party or for any other reason,

the licensor may have the right to terminate the license, in which event we may not be able to market any product that is covered by the licensed patents. In addition, the failure to comply with our obligations under our license agreement with University of South Florida Research Foundation or our license agreement with Yale University could constitute a breach of our obligations under our 2009 agreement with AstraZeneca. A material breach by us of our 2009 agreement with AstraZeneca would give rise to various remedies for AstraZeneca that could have a material adverse effect on our business.

Our patent protection for any particular compound may be limited to a specific method of use or indication. If a third party were to obtain approval of a particular compound for use in another indication, we could be subject to competition arising from off-label use.

Although we generally seek the broadest patent protection available for our compounds, we or any of our applicable collaborators may not be able to obtain patent protection for the actual composition of any particular compound and may be limited to protecting a new method of use for the compound or otherwise restricted in our ability to prevent others from exploiting the compound. If we or any of our applicable collaborators are unable to obtain patent protection for the actual composition of any compound that we seek to develop and commercialize and must rely on method of use patent coverage, we would likely be unable to prevent others from manufacturing or marketing that compound for any use that is not protected by our patent rights. If a third party were to receive marketing approval of any compound for which we rely on method of use patent coverage for another use, physicians could nevertheless prescribe it for indications that are not described in the product's labeling or approved by the FDA or foreign regulatory authorities. Even if we have patent protection for the indication for which the product is prescribed, as a practical matter, we would have little recourse as a result of this off-label use. In that event, our revenue from the commercialization of the compound would likely be materially and adversely affected.

If a third party were to obtain approval to market and sell mecamylamine hydrochloride, TC-5214 could be subject to competition arising from off-label use.

We have licensed patent rights in the United States covering the pharmaceutical composition and methods of use of TC-5214, one of the enantiomers of mecamylamine hydrochloride. We have licensed method of use patent rights for, but do not have patent rights covering the composition of, mecamylamine hydrochloride. As a result, we may be limited in our ability to prevent others from exploiting mecamylamine, which could have a negative impact on the commercial potential of TC-5214. We believe there are at least three companies that are currently developing mecamylamine: CoMentis, Inc., which we believe is developing mecamylamine in an eye drop formulation as a treatment for age-related macular degeneration, a condition characterized by degeneration of the retina in the eye; AGI Therapeutics Ltd., which we believe is developing mecamylamine for chemotherapy-induced diarrhea; and Cary Pharmaceuticals Inc., which we believe is developing mecamylamine in a fixed dose combination with bupropion as a smoking cessation aid. In addition, mecamylamine is the active ingredient in our approved product Inversine, which we have discontinued. A third party could in the future pursue marketing approval of mecamylamine for the forms of hypertension for which Inversine is approved using the abbreviated new drug application process. If any third party were to receive marketing approval for mecamylamine for any indication, physicians could prescribe it for other indications that are not described in the product's labeling or approved by the FDA or foreign regulatory authorities. In particular, physicians could potentially prescribe mecamylamine as a treatment for major depressive disorder. In that event, if TC-5214 is in the future approved for marketing and sale by the FDA or foreign regulatory authorities, our revenue from sales of TC-5214 would likely be materially and adversely affected.

We may be involved in lawsuits to protect or enforce our patents that could be expensive and time-consuming.

We may initiate patent litigation against third parties to protect or enforce our patent rights and we may be similarly sued by third parties. We may also become subject to interference or opposition proceedings conducted in the patent and trademark offices of various countries to determine our entitlement to patents. The defense and

prosecution of intellectual property suits, interference proceedings and related legal and administrative proceedings, if necessary, would be costly and divert our technical and management personnel from conducting our business. Moreover, we may not prevail in any of these suits. An adverse determination of any litigation or proceeding could put our patents at risk of being invalidated or narrowly interpreted and our patent applications at risk of not being issued and could prevent us from protecting our rights, particularly in countries where the laws may not protect such rights as fully as in the United States.

Furthermore, because of the substantial amount of discovery required in connection with intellectual property litigation, there is a risk that disclosure of some of our confidential information could be compelled and the information compromised. In addition, during the course of this kind of litigation, there could be public announcements of the results of hearings, motions or other interim proceedings or developments that, if perceived as negative by securities analysts or investors, could have a material adverse effect on the trading price of our common stock.

Claims by third parties that we infringe their proprietary rights may result in liability for damages or prevent or delay our development and commercialization efforts.

Our success depends in part on avoiding the infringement of other parties' patents and proprietary rights. Patents may issue from patent applications of which we are unaware, and avoiding patent infringement may be difficult. We may infringe or it may be alleged that we infringe third-party patents. If a third party were to file a patent infringement suit against us, we could be forced to stop or delay research, development, manufacturing or sales of any infringing product in the country or countries covered by the patent infringed, unless we can obtain a license from the patent holder. Any necessary license may not be available on acceptable terms or at all, particularly if the third party is developing or marketing a product competitive with the infringing product. Even if we are able to obtain a license, the rights may be nonexclusive, which would give our competitors access to the same intellectual property.

We also may be required to pay substantial damages to the patent holder in the event of an infringement. These damages could in some circumstances be triple the actual damages the patent holder incurs. If we have supplied infringing products to third parties for marketing or have licensed third parties to manufacture, use or market infringing products, we may be obligated to indemnify these third parties for any damages they may be required to pay to the patent holder and for any losses they may sustain themselves as a result.

Any successful infringement action brought against us may also materially and adversely affect marketing of the infringing product in other markets not covered by the infringement action, as well as our marketing of other products based on similar technology. Furthermore, we may suffer material adverse consequences from a successful infringement action against us even if the action is subsequently reversed on appeal, nullified through another action or resolved by settlement with the patent holder. The damages or other remedies awarded, if any, may be significant. As a result, any infringement action against us would likely delay the regulatory approval process, harm our competitive position, be very costly and require significant time and attention of our key management and technical personnel.

Risks Related to Commercialization

Even if approved for marketing and sale, our product candidates may not gain market acceptance and may fail to generate significant revenue.

The commercial success of any of our product candidates for which we may obtain marketing approval from the FDA or other regulatory authorities will depend upon their acceptance by the medical community and third-party payors as clinically useful, cost-effective and safe. Many of the product candidates that we are developing are based upon technologies or methods of treatment that are relatively new and unproven. As a result, it may be more difficult for us to achieve market acceptance of our products.

The degree of market acceptance of any drug depends on a number of factors, such as:

- its demonstration of efficacy and safety in clinical trials;
- its superior efficacy as compared to alternative treatment methods and its side effect profile;
- its cost-effectiveness and the availability of insurance or other third-party reimbursement;
- its convenience and ease of administration;
- the timing of its market entry relative to competitive treatments;
- the extent and success of marketing and sales efforts; and
- the product labeling or product insert required by the FDA or regulatory authorities in other countries.

In addition, perceptions about the relationship or similarity between our product candidates and nicotine could limit their market potential. Our product candidates derive their medical effects by interacting with NNRs. Nicotine, which can have significantly negative health effects, also interacts with NNRs. Accordingly, our product candidates may be perceived by some to be nicotine or to be closely related to nicotine, particularly in light of the shared derivative names, “nicotine” and neuronal “nicotinic” receptors, and the fact that our company was launched originally as a research group within, and then as a subsidiary of, R.J. Reynolds Tobacco Company. This potential perception could result in a reluctance by patients to take, or by physicians to prescribe, any of our product candidates that receives marketing approval, which would affect our revenue.

We currently have limited sales, marketing and distribution experience and no internal sales or distribution capabilities. If we are unable to enter into alliances and collaborations or other arrangements with third parties to market and sell our product candidates or to develop our own internal marketing capability, or if we enter into such arrangements with third parties who do not perform well, we may not be successful in commercializing our products.

We currently have limited sales, marketing and distribution experience and no internal sales or distribution capabilities. Although we intend to focus any future internal sales and marketing resources in areas where specialists heavily influence our target markets, such as neurology and psychiatry, we also intend to seek to further augment our sales, marketing and distribution capabilities through arrangements with third parties such as our collaborations with AstraZeneca and our alliance with GlaxoSmithKline. In particular, our strategy includes selectively entering into strategic alliances and collaborations with respect to product candidates for indications with sales and distribution characteristics requiring a large sales force. There are risks involved with establishing our own sales force and marketing and distribution capabilities, as well as in entering into arrangements with third parties to perform these services. Developing our own sales force would be expensive and time-consuming and could delay any product launch. We may not be successful in entering into arrangements with third parties on terms that are favorable to us or at all. Also, we have little control over AstraZeneca and GlaxoSmithKline and would have little control over such other third parties, any of which may fail to devote the necessary resources and attention to sell, market or distribute our products effectively. If we do not establish sales and distribution capabilities successfully, either on our own or in collaboration with third parties, we may not successfully commercialize our products.

Unfavorable pricing regulations, third-party reimbursement practices or healthcare reform initiatives applicable to our product candidates could limit our potential product revenue.

The regulations governing drug pricing and reimbursement vary widely from country to country. Some countries require approval of the sale price of a drug before it can be marketed and, in many of these countries, the pricing review period begins only after approval is granted. In some countries, prescription pharmaceutical pricing remains subject to continuing governmental control even after initial approval is granted. Our product candidates are currently in the development stage and we cannot yet assess the impact of price regulations. As a result, we or any applicable collaborator of ours may obtain regulatory approval for a product in a particular country, but then be subject to price regulations that delay the commercial launch of the product and may negatively impact the revenue we are able to derive from sales in that country.

Successful commercialization of any of our product candidates that is successfully developed will also depend in part on the extent to which coverage and adequate payment is available from government health administration authorities, private health insurers and other third-party payors. If we or any applicable collaborator of ours succeeds in bringing a product candidate to the market, it may not be considered cost-effective and reimbursement to the patient may not be available or sufficient to allow us or the collaborator to sell it at a satisfactory price. Because our product candidates are in the development stage, we cannot yet determine their cost-effectiveness. We may need to conduct expensive studies in order to demonstrate cost-effectiveness. Moreover, third-party payors frequently require that pharmaceutical companies provide predetermined discounts from list prices and frequently challenge the prices charged for medical products. Because our product candidates are in the development stage, we do not yet know the level of reimbursement, if any, for any product candidates that we or any applicable collaborator of ours are able to successfully develop. If the reimbursement for any of our product candidates is inadequate in light of our development and other costs, our ability to achieve or sustain profitability could be materially and adversely affected.

We believe that the efforts of governments and third-party payors to contain or reduce the cost of healthcare will continue to affect the business and financial condition of pharmaceutical and biopharmaceutical companies. The U.S. Congress has been actively debating healthcare reform for some time, and the House and the Senate have passed different healthcare reform bills. These bills and other ongoing initiatives in the United States have and will continue to increase pressure on the delivery of healthcare generally and on drug pricing in particular. If these bills are reconciled or if another version of healthcare reform is enacted into law, such a law could have a material adverse effect on potential revenue from any product candidate that we or any applicable collaborator of ours may successfully develop.

A number of legislative and regulatory proposals to change the healthcare system in the United States and other major healthcare markets have been proposed and adopted in recent years. For example, The American Recovery and Reinvestment Act of 2009, which became effective in February 2009, provides funding for the federal government to compare the effectiveness of different treatments for the same illness. A plan for the research is to be developed by the Department of Health and Human Services, the Agency for Healthcare Research and Quality and the National Institutes for Health, and periodic reports on the status of the research and related expenditures are to be made to the U.S. Congress. Although the results of the comparative effectiveness studies are not intended to mandate any policies for public or private payors, it is unclear what if any effect the research will have on the sales of any product candidate that we or any applicable collaborator of ours successfully develops if the product candidate or the condition that it is intended to treat is the subject of the research. Decreases in third-party reimbursement for any of our product candidates that is successfully developed or a decision by a third-party payor to not cover any of our product candidates that is successfully developed could reduce prescriptions by physicians of the product candidate and have a material adverse effect on our potential revenue from sales of the product candidate.

If our competitors develop and market drugs that are less expensive, more effective or safer than ours, if they develop and market products faster than we do, or if they have better sales and marketing capabilities than we do, any products we are able to commercialize may not generate initial or ongoing revenue.

The development and commercialization of new drugs is highly competitive. Our business is characterized by extensive research efforts and rapid developments. We expect intense competition in our target markets as new products and advanced technologies become available. Our competitors include large pharmaceutical, biopharmaceutical, biotechnology and other companies and research institutions, many of which have greater financial, technical and other resources and personnel and more experience in research, clinical development, regulatory and drug commercialization than we have. Our competitors may:

- develop products that are more effective, safer, more tolerable, more convenient, less costly or otherwise more competitive than our product candidates;
- obtain FDA or foreign regulatory approval for their products more rapidly than we or any applicable collaborator of ours does;

- adapt more quickly to new technologies and scientific advances than we or any applicable collaborator of ours;
- initiate or withstand substantial price competition more successfully than we or any applicable collaborator of ours does;
- have greater success in recruiting skilled scientific workers from the limited pool of available talent than we do;
- obtain more effective intellectual property protection than we have;
- negotiate third-party licensing and collaboration arrangements more effectively than we do; and
- take advantage of acquisition or other opportunities more readily than we do.

Competitive products may render our product candidates obsolete or noncompetitive before we can recover our development or commercialization expenses.

We also face substantial competition from therapies designed to target NNRs. Pfizer's product Chantix, which is known outside of the United States as Champix, acts on several NNR subtypes as well as other molecular targets in the body. Chantix is approved as an aid for smoking cessation. In addition, we believe that several prominent pharmaceutical companies have product candidates that target NNRs in development, including as examples Roche, with a compound in Phase 2 development for Alzheimer's disease and cognitive impairment associated with schizophrenia (which we refer to as cognitive dysfunction in schizophrenia), and Abbott Laboratories, with one compound in Phase 2 development for Alzheimer's disease and ADHD, a second compound in Phase 2 development for ADHD and a third compound in Phase 1 development for cognitive disorders. Other companies that we believe have active NNR-based programs include AstraZeneca, Eli Lilly, Sanofi-Aventis, Wyeth, Bristol Myers Squibb, GlaxoSmithKline, Johnson & Johnson, Novartis, NeuroSearch A/S, Solvay, Servier, CoMentis, EnVivo Pharmaceuticals, Xytis and Galantos Pharma. We expect that we will face increased competition in the future if therapies that target NNRs are further validated and if companies initiate or expand programs focused on NNRs or otherwise enter the CNS market, whether independently or by alliance, collaboration or acquisition.

Any products that we or any applicable collaborator of ours is able to successfully develop and commercialize in the future could be subject to competition from lower priced generic drugs. The manufacturer of a generic product could challenge our patents as invalid or not infringed and subject us to expensive litigation. We do not know if we or any applicable collaborator of ours would prevail in litigation and succeed in keeping the generic product out of the market until our patent protection expires.

If we successfully develop and obtain approval for our product candidates, we will face competition based on the safety and effectiveness of our products, the timing and scope of regulatory approvals, the availability and cost of supply, marketing and sales capabilities, reimbursement coverage, price, patent position and other factors. Our competitors may develop or commercialize more effective or more affordable products, or obtain more effective patent protection, than we do. Accordingly, our competitors may commercialize products more rapidly or effectively than we do.

If approved, our product candidates will compete for a share of the existing market with numerous approved products. We believe that the primary competitive products for use in indications that we are currently targeting with our most advanced product candidates include:

- for major depressive disorder, selective serotonin reuptake inhibitors such as Prozac from Eli Lilly, Paxil from GlaxoSmithKline, Zoloft from Pfizer, Celexa and Lexapro from Forest Laboratories, dual uptake inhibitors such as Effexor from Wyeth and Cymbalta from Eli Lilly and, as an adjunctive treatment, the atypical antipsychotics Seroquel XR from AstraZeneca and Abilify from Bristol-Myers Squibb/Otsuka;

- for ADHD, stimulants such as Adderall XR and Vyanase from Shire, Concerta from Johnson & Johnson and Ritalin LA from Novartis, and Strattera, a non-stimulant acting as a norepinephrine reuptake inhibitor, from Eli Lilly; and
- for mild to moderate Alzheimer's disease, acetylcholinesterase inhibitors such as Aricept from Pfizer/Eisai, Razadyne from Johnson & Johnson and Exelon from Novartis; in addition, Namenda from Forest Laboratories, which acts by regulating the neurotransmitter glutamate, is marketed for moderate to severe Alzheimer's disease.

There is currently no approved product for cognitive dysfunction in schizophrenia.

We may have substantial exposure to product liability claims and may not have adequate insurance to pay them.

We face an inherent business risk of exposure to product liability claims if the use of our products is alleged to have resulted in harm to others. This risk exists for product candidates in clinical trials, whether or not the product candidate is subsequently approved for commercial sale, as well as for products in commercial distribution. Any product liability claim arising in the future against us or any third party that we have agreed to indemnify, regardless of its merit or eventual adjudication, could be costly and significantly divert management's attention from conducting our business or materially and adversely affect our reputation and the demand for our products.

We have secured product liability insurance coverage in amounts that we believe to be appropriate for our current operations. Our current insurance coverage may not reimburse us or may not be sufficient to reimburse us for any expenses or losses we may incur. We expect that we will expand our coverage with respect to any products for which we obtain marketing approval. However, additional insurance may not be available to cover our potential liabilities fully or may be prohibitively expensive. In addition, some potential product liability claims may be excluded from coverage under the terms of the policy. Our inability to obtain adequate insurance coverage at an acceptable cost could prevent or impede the commercialization of our product candidates.

Our business activities involve hazardous materials, which could subject us to significant liability.

Our research and development activities involve, and any future manufacturing processes that we conduct may involve, the use of hazardous materials, including hazardous chemicals and radioactive materials. Accordingly, we are subject to federal, state and local laws and regulations governing the use, manufacture, storage, handling and disposal of these materials. We incur significant costs in our efforts to comply with these laws and regulations, but our efforts may not ensure compliance in all cases. Moreover, despite precautionary procedures that we implement, we cannot eliminate the risk of accidental contamination or injury from these materials. In the event of an accident or environmental discharge, we may be held liable for any resulting damages. We do not carry insurance specifically for the risk of contamination or injury from hazardous materials.

If any promotional activities that we undertake fail to comply with the regulations and guidelines of the FDA and other applicable regulatory authorities, we may be subject to warnings or enforcement actions that could harm our business.

Physicians may prescribe drugs for uses that are not described in the product's labeling or for uses that differ from those tested in clinical studies and approved by the FDA or similar regulatory authorities in other countries. Regulatory authorities generally do not regulate the behavior of physicians in their choice of treatments. Regulatory authorities do, however, restrict communications on the subject of off-label use. Companies cannot actively promote approved drugs for off-label uses but may in some jurisdictions and under specified conditions disseminate articles published in peer-reviewed journals that discuss off-label uses of approved products to physicians. To the extent allowed, we may in the future disseminate peer-reviewed articles

on our products to physicians. If we undertake any promotional activities in the future for any product candidate for which we receive regulatory approval and our activities fail to comply with these regulations or guidelines, we may be subject to warnings from, or enforcement action by, these authorities.

Risks Related to Employees and Managing Growth

If we lose our key personnel or are unable to attract and retain additional skilled personnel, we may be unable to successfully develop and commercialize our product candidates or effectively compete in our industry.

Our performance depends substantially on the performance of our senior management and key scientific, technical and managerial personnel, including our Chief Executive Officer and President, J. Donald deBethizy, and our Vice President, Clinical Development and Regulatory Affairs, Geoffrey C. Dunbar. Our executive officers, including these individuals, can terminate their employment with us at any time. The loss of the services of any of our executive officers may significantly delay or prevent the achievement of product research and development and other business objectives. We also rely on consultants and advisors from time to time to assist us in formulating our research and development strategy. All of our consultants and advisors are either self-employed or employed by other organizations, and they may have other commitments, including consulting or advisory contracts with other organizations, that may affect their ability to contribute to us.

Our ability to operate successfully and manage our potential future growth will depend on our ability to identify, recruit and retain additional qualified scientific, technical, financial and managerial personnel. We face intense competition for skilled executives in our industry. We may not be able to continue to attract and retain personnel with the advanced qualifications necessary for the growth of our business.

We may encounter difficulties in managing our growth, which could increase our losses.

The number of our employees and the scope of our operations have grown over the last several years. Any continued growth could place a significant strain on our managerial, operational and financial resources. To manage our growth, we must continue to implement and improve our managerial, operational and financial systems and controls and reporting processes and procedures. We may not be able to manage our growth effectively. Moreover, if our existing systems and internal controls over financial reporting are not implemented properly or are not adequate, we could be exposed to an increased risk of incurring financial or accounting irregularities or fraud, which would cause our stock price to suffer.

Risks Related to Our Common Stock

The market price of our common stock may be highly volatile.

We expect that the trading price of our common stock is likely to be highly volatile in response to factors that are beyond our control. The stock market in general has experienced extreme price and volume fluctuations. The market prices of securities of pharmaceutical, biopharmaceutical and biotechnology companies have been extremely volatile and have experienced fluctuations that have often been unrelated or disproportionate to operating performance. These broad market fluctuations could result in extreme fluctuations in the price of our common stock, which could cause a decline in the value of shares held by any stockholder.

If our operating results fluctuate significantly, our stock price may decline.

Our operating results are likely to fluctuate significantly from quarter to quarter and year to year. These fluctuations could cause our stock price to decline. Some of the factors that could cause our operating results to fluctuate include:

- whether and to what extent milestone events are achieved for TC-5214 under our December 2009 agreement with AstraZeneca and for AZD3480 or AZD1446 under our December 2005 agreement with AstraZeneca;

- whether, following our completion of our ongoing Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia, AstraZeneca exercises its right to license TC-5619;
- the scope, progress, duration, results and cost of clinical trials, as well as non-clinical studies and assessments, of our product candidates;
- the extent to which our research and development activities in the programs that are the therapeutic focus areas of our alliance with GlaxoSmithKline result in the achievement of milestone events under our alliance agreement;
- the extent to which we retain development and commercialization rights or responsibilities for our product candidates that are not subject to either of our collaborations with AstraZeneca or to our alliance with GlaxoSmithKline and incur associated development and manufacturing costs and costs to establish sales and marketing functions;
- our ability to establish strategic alliances, collaborations and licensing or other arrangements on terms favorable to us;
- our inability, or the inability of AstraZeneca, GlaxoSmithKline or any potential future collaborator, to successfully complete clinical trials or non-clinical studies and assessments in a timely manner or at all, resulting in a delay in receiving, or a failure to receive, the required regulatory approvals to commercialize our product candidates;
- the cost, timing and outcomes of regulatory approvals or other regulatory actions;
- the number and characteristics of product candidates that we pursue;
- general and industry-specific economic conditions that may affect the research and development expenditures of AstraZeneca, GlaxoSmithKline or any of our potential future collaborators;
- the expiration or termination of agreements with AstraZeneca, GlaxoSmithKline or any potential future collaborator, or the execution of new agreements; and
- general conditions in the pharmaceutical, biopharmaceutical or biotechnology industries or in the U.S. or global credit or financial markets.

Due to fluctuations in our operating results, a period-to-period comparison of our results of operations may not be a good indication of our future performance. In any particular quarter or quarters, our operating results could be below the expectations of securities analysts or investors and our stock price could decline.

If our stockholders sell a substantial number of shares of our common stock in the public market, our stock price may decline.

Our current trading volumes are modest, and sales of a substantial number of shares of our common stock in the public market could cause the market price to decline. Such sales also might make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. If there are more shares of our common stock offered for sale than buyers are willing to purchase, the market price of our common stock may decline to a market price at which buyers are willing to purchase the offered shares and sellers remain willing to sell the shares. The number of shares of our common stock owned by our stockholders and available for sale in the public market is limited only to the extent provided under applicable federal securities laws. In addition, we may, in the future, issue additional shares of our common stock as compensation to our employees, directors or consultants, in connection with strategic alliances, collaborations or acquisitions or to raise capital. Accordingly, sales of a substantial number of shares of our common stock in the public market could occur at any time.

Concentration of ownership among our existing executive officers, directors and principal stockholders may prevent new investors from influencing significant corporate decisions.

Our executive officers, directors and 10% or greater stockholders beneficially own or control approximately 43% of the outstanding shares of our common stock, based on the shares outstanding as of February 28, 2010. Accordingly, our executive officers and directors and these principal stockholders have substantial control over the outcome of corporate actions requiring stockholder approval, including the election of directors, any merger, consolidation or sale of all or substantially all of our assets or any other significant corporate transactions, as well as our management and affairs. The concentration of ownership may also delay or prevent a change of control of us at a premium price if these stockholders oppose it, even if it would benefit our other stockholders.

Provisions of our charter, bylaws and Delaware law may make an acquisition of us or a change in our management more difficult.

Provisions of our certificate of incorporation and bylaws could discourage, delay or prevent a merger, acquisition or other change in control that stockholders may consider favorable, including transactions in which stockholders might otherwise receive a premium for their shares. These provisions also could limit the price that investors might be willing to pay in the future for shares of our common stock, thereby depressing the market price of our common stock. Stockholders who wish to participate in these transactions may not have the opportunity to do so. Furthermore, these provisions could prevent or frustrate attempts by our stockholders to replace or remove our management. These provisions:

- allow the authorized number of directors to be changed only by resolution of our board of directors;
- establish a classified board of directors, providing that not all members of the board be elected at one time;
- authorize our board of directors to issue without stockholder approval blank check preferred stock that, if issued, could operate as a “poison pill” to dilute the stock ownership of a potential hostile acquirer to prevent an acquisition that is not approved by our board of directors;
- require that stockholder actions must be effected at a duly called stockholder meeting and prohibit stockholder action by written consent;
- establish advance notice requirements for stockholder nominations to our board of directors or for stockholder proposals that can be acted on at stockholder meetings;
- limit who may call stockholder meetings; and
- require the approval of the holders of 66 2/3% of the outstanding shares of our capital stock entitled to vote in order for the stockholders to amend certain provisions of our certificate of incorporation and bylaws.

In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which may, unless certain criteria are met, prohibit large stockholders, in particular those owning 15% or more of our outstanding voting stock, from merging or combining with us for a prescribed period of time.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

We lease approximately 58,000 square feet of laboratory and office space located in the Piedmont Triad Research Park in Winston-Salem, North Carolina. We also have rights exercisable at any time during the remaining term of the lease to lease additional space in this facility upon twelve months notice. The term of our

lease expires July 31, 2012, and we have a renewal option for an additional five-year term at a rental rate to be mutually determined. The current monthly payment under our lease is approximately $180,000. We believe our laboratory and office space is suitable for its intended purpose. We expect that we may require additional space within the next two years and are considering alternatives for such space, including our right to lease additional space in our current facility.

Item 3. Legal Proceedings.

We are not currently a party to any material pending legal proceedings or aware of any contemplated proceeding against us by any governmental authority.

Item 4. (Removed and Reserved).

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information

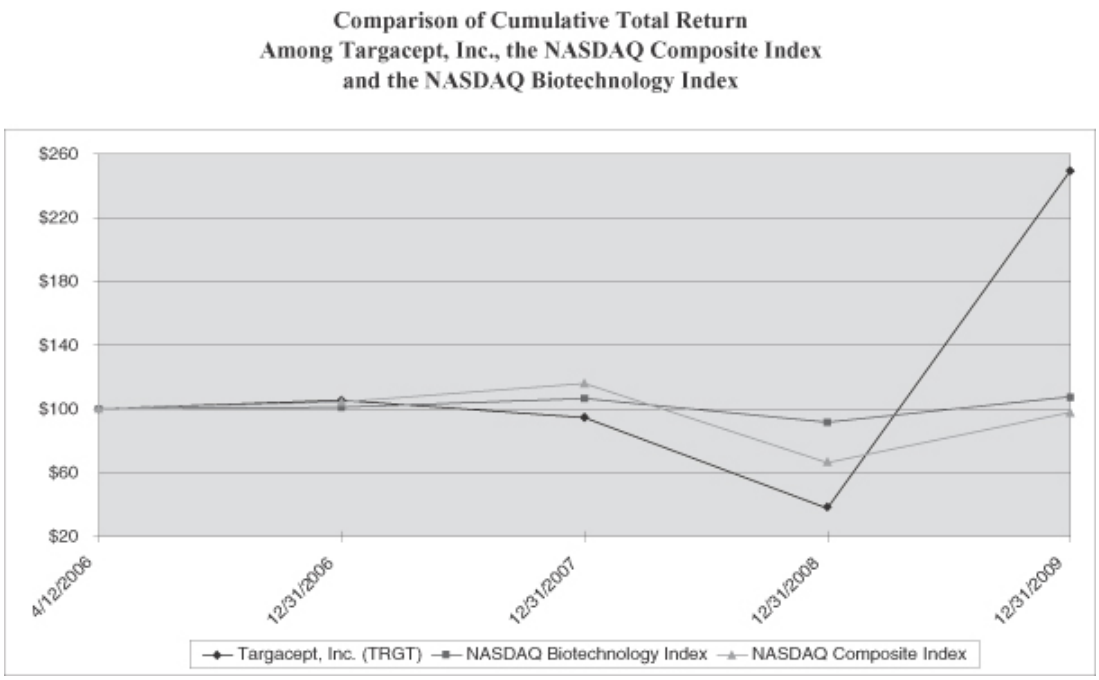
Our common stock trades on the NASDAQ Global Market under the symbol "TRGT." The following table sets forth, for the periods indicated, the high and low sales prices for our common stock:

	Common Stock	
	High	*Low*
2008:		
First Quarter	$ 8.61	$ 6.81
Second Quarter	$ 8.50	$ 6.90
Third Quarter	$ 10.11	$ 3.85
Fourth Quarter	$ 6.19	$ 1.40
2009:		
First Quarter	$ 3.94	$ 2.00
Second Quarter	$ 4.17	$ 2.26
Third Quarter	$ 21.84	$ 2.00
Fourth Quarter	$ 24.50	$ 17.59

Comparative Stock Performance Graph

The following graph and related information shall not be deemed "soliciting material" or to be "filed" with the SEC or subject to Regulation 14A or 14C, other than as provided in Item 201 of Regulation S-K, or to the liabilities of Section 18 of the Exchange Act, nor shall such information be incorporated by reference into any future filing under the Securities Act or the Exchange Act, except to the extent that we specifically incorporate it by reference into such a filing.

The following graph compares the cumulative total stockholder return for our common stock with the cumulative total stockholder return of the NASDAQ Composite Index and the NASDAQ Biotechnology Index. The comparison assumes the investment of $100.00 on April 12, 2006 (the date our common stock was first publicly traded) in each of our common stock, the NASDAQ Composite Index and the NASDAQ Biotechnology Index and the reinvestment of any dividends. We have not paid any dividends on our common stock and do not include dividends in the representation of our performance. The performance shown for any prior period does not predict the performance to be expected for the current period or any future period.



	Cumulative Total Return				
	4/12/06	12/31/06	12/31/07	12/31/08	12/31/09
Targacept, Inc.	100	105	95	41	241
NASDAQ Biotechnology Index	100	101	106	92	107
NASDAQ Composite Index	100	104	115	68	98

Stockholders

As of February 28, 2010, there were approximately 64 holders of record of our common stock. Because many of our shares are held by brokers or other nominees on behalf of beneficial owners, we are unable to determine precisely the total number of beneficial owners represented by the holders of record. As of February 28, 2010, we estimate the total number of beneficial owners of our common stock whose shares are held by brokers or other nominees on their behalf to be approximately 3,525.

Dividends

We have never declared or paid cash dividends on any of our shares of capital stock. We currently intend to retain future earnings, if any, to finance the expansion and growth of our business and do not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be at the discretion of our board of directors and will depend on our financial condition, results of operations, capital requirements and other factors that our board of directors deems relevant. In addition, the terms of any future debt or credit facility may preclude us from paying dividends.

Calculation of Aggregate Market Value of Non-Affiliate Shares

For purposes of calculating the aggregate market value of shares of our common stock held by non-affiliates as set forth on the cover page of this annual report, we have assumed that all outstanding shares are held by non-affiliates, except for shares held by our executive officers, directors and stockholders that hold at least 10% of our outstanding common stock as of the determination date. This assumption is not intended to constitute an admission that all executive officers, directors and 10% or greater stockholders are, in fact, our affiliates or that there are not other persons who may be deemed to be our affiliates.

Unregistered Sales of Securities; Use of Proceeds from Registered Securities; Issuer Purchases of Equity Securities

None.

Item 6. Selected Financial Data.

You should read the following selected financial data together with our financial statements and the related notes included in this annual report and the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of this annual report. The selected financial data in this section are not intended to replace our financial statements.

We derived the statements of operations data for the years ended December 31, 2009, 2008 and 2007 and the balance sheet data as of December 31, 2009 and 2008 from our audited financial statements included in this annual report. We derived the statements of operations data for the years ended December 31, 2006 and 2005 and the balance sheet data as of December 31, 2007, 2006 and 2005 from our audited financial statements not included in this report. Our historical results for any prior period are not necessarily indicative of the results to be expected for any future period. You should read the notes to our financial statements for an explanation of the method used to determine the number of shares used in computing basic and diluted net loss per share.

	Year Ended December 31,				
	2009	2008	2007	2006	2005
	(in thousands, except share and per share data)				
Statement of Operations Data:					
Net operating revenues	$ 25,062	$ 20,085	$ 11,576	$ 27,537	$ 1,180
Operating expenses:					
Research and development	40,179	40,981	34,620	21,788	24,252
General and administrative	8,167	6,499	8,013	5,696	4,753
Transaction charges	—	—	—	—	1,635
License fees and royalties	16,350	—	—	—	—
Cost of product sales	691	749	715	457	481
Total operating expenses	65,387	48,229	43,348	27,941	31,121
Loss from operations	(40,325)	(28,144)	(31,772)	(404)	(29,941)
Interest and dividend income	1,050	2,734	3,837	2,584	1,174
Interest expense	(217)	(251)	(138)	(83)	(225)
(Loss) income before income taxes	(39,492)	(25,661)	(28,073)	2,097	(28,992)
Income tax benefit	88	—	—	—	—
Preferred stock accretion	—	—	—	(3,333)	(11,238)
Net loss attributable to common stockholders	$ (39,404)	$ (25,661)	$ (28,073)	$ (1,236)	$ (40,230)
Basic and diluted net loss attributable to common stockholders per share	$ (1.54)	$ (1.04)	$ (1.42)	$ (0.09)	$ (153.54)
Weighted average common shares outstanding—basic and diluted	25,636,419	24,664,169	19,720,732	13,595,523	262,013

	As of December 31,				
	2009	2008	2007	2006	2005
	(in thousands)				
Balance Sheet Data:					
Cash, cash equivalents and short-term investments	$ 111,066	$ 88,363	$ 87,040	$ 54,190	$ 24,851
Working capital	213,269	78,174	77,217	69,903	20,531
Total assets	319,379	98,551	98,965	81,368	28,001
Long-term debt, net of current portion	1,966	3,408	1,686	816	1,409
Redeemable convertible preferred stock	—	—	—	—	183,628
Accumulated deficit	(229,300)	(189,896)	(164,235)	(136,162)	(174,983)
Total stockholders' equity (deficit)	68,991	57,373	51,584	64,999	(162,481)

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes included in this annual report. In addition to historical information, the following discussion contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results, performance or experience could differ materially from those indicated by any forward-looking statement due to various important factors, risks and uncertainties, including, but not limited to, those set forth under "Cautionary Note Regarding Forward-Looking Statements," which precedes Part I of this annual report, and under "Risk Factors" in Item 1A of Part I of this annual report.

Overview

Background

We are a biopharmaceutical company engaged in the design, discovery and development of novel NNR Therapeutics for the treatment of diseases and disorders primarily of the central nervous system. Our NNR Therapeutics selectively target a class of receptors known as neuronal nicotinic receptors, which we refer to as NNRs. NNRs are found on nerve cells throughout the nervous system and serve as key regulators of nervous system activity. Our most advanced product candidates are TC-5214, AZD3480 (TC-1734), AZD1446 (TC-6683), TC-5619 and TC-6987 and are discussed under the caption "Business" in Item 1 of Part I of this annual report.

We have two collaboration agreements with AstraZeneca, one that we entered into in December 2009 for the global development and commercialization of TC-5214 as a treatment for major depressive disorder and refer to in this annual report as our "2009 agreement with AstraZeneca" and the other focused in cognitive disorders that we entered into in December 2005 and refer to in this annual report as our "2005 agreement with AstraZeneca."

Under our 2009 agreement with AstraZeneca, we and AstraZeneca have jointly designed an initial development program that is planned to include development of TC-5214 as an adjunct therapy and as a second-line "switch" monotherapy, in each case in adults with major depressive disorder who do not respond adequately to first-line antidepressant treatment. AstraZeneca is responsible for 80% of the cost of the initial program, except that AstraZeneca is responsible for 100% of development costs that are required only to obtain or maintain regulatory approval in countries outside the United States and the European Union. We are responsible for 20% of the costs of the initial program but have the right to terminate our obligation to fund our share of these costs once we have funded a specified amount. If we fund the specified amount and terminate our obligation to fund our share of further costs of the initial development program, any future milestones and royalties payable to us under the agreement would be reduced by the amount of our unfunded share plus interest, subject to a maximum reduction that may be applied to any one payment. AstraZeneca is responsible for executing and funding the costs of global commercialization of TC-5214.

Under our 2005 agreement with AstraZeneca, we and AstraZeneca conducted a preclinical research collaboration that was designed to discover and develop compounds that act on the a4ß2 NNR as treatments for conditions characterized by cognitive impairment. AstraZeneca paid us research fees, based on a reimbursement rate specified under the agreement, for research services rendered in the preclinical research collaboration, subject to specified limits. The research term began in January 2006, had a planned term of four years and expired in January 2010. In addition, AstraZeneca is responsible under the terms of the agreement for substantially all current and future development costs for AZD3480 and compounds that arose from the preclinical research collaboration, except for costs to conduct the Phase 2 clinical trial of AZD3480 in adults with ADHD that we completed in June 2009.

In addition to our collaboration with AstraZeneca, we have a strategic alliance with GlaxoSmithKline that is designed to discover, develop and market product candidates that selectively target specified NNR subtypes in specified therapeutic focus areas.

We trace our scientific lineage to a research program initiated by R.J. Reynolds Tobacco Company in 1982 to study the activity and effects of nicotine in the body. We were incorporated in 1997 as a wholly owned subsidiary of RJR. In August 2000, we became an independent company when we issued and sold stock to venture capital investors. Since our inception, we have had limited revenue from product sales and have funded our operations principally through the sale of equity securities, revenue from collaboration agreements, grants and equipment and building lease incentive financing. We have devoted substantially all of our resources to the discovery and development of our product candidates and technologies, including the design, conduct and management of preclinical and clinical studies and related manufacturing, regulatory and clinical affairs, as well as intellectual property prosecution.

We generated net income for the third quarter ended September 30, 2009 and for the fourth quarter and year ended December 31, 2006, in each case due primarily to the achievement in each period of a single milestone event related to AZD3480 under our 2005 agreement with AstraZeneca. Except for these periods, we have never been profitable. As of December 31, 2009, we had an accumulated deficit of $229.3 million. We may incur losses for the foreseeable future as our clinical-stage and preclinical product candidates advance into later-stage development, as we progress our programs, invest in additional product opportunities and expand our research and development infrastructure. Clinical trials and preclinical studies are time-consuming, expensive and may never yield a product that will generate revenue.

A substantial portion of our revenue is derived from recognition of deferred license fees and depends on the successful achievement of milestone events under our agreements with AstraZeneca and GlaxoSmithKline and, as a clinical-stage company, our revenues, expenses and results of operations are likely to fluctuate significantly from quarter to quarter and year to year. We believe that period-to-period comparisons of our results of operations should not be relied upon as indicative of our future performance.

Revenue

Under our 2009 agreement with AstraZeneca, we received a $200.0 million upfront payment in January 2010. We are eligible to receive additional payments of over $1.0 billion if development, regulatory, first commercial sale and specified sales related milestones are achieved and stepped double-digit royalties on any future product sales.

As of December 31, 2009, we had received $44.4 million in aggregate upfront fees and milestone payments under our 2005 agreement with AstraZeneca and had recognized an additional $26.5 million in collaboration research and development revenue for research services that we provided in the preclinical research collaboration that we conducted with AstraZeneca under that agreement. We are eligible to receive other payments of up to $103.0 million, if development, regulatory, first commercial sale and first detail milestones are achieved for AZD3480 only for ADHD, and stepped double-digit royalties on any future product sales. If AZD3480 is developed under the agreement for an indication in addition to ADHD, we would also be eligible to receive additional milestone payments upon the achievement of development, regulatory, first commercial sale and first detail milestones for AZD3480 for each such indication.

In addition, we are eligible to receive payments of up to $108.0 million, contingent upon the achievement of development, regulatory, first commercial sale and first detail milestones for AZD1446 for two indications, and stepped royalties on any future AZD1446 product sales. Also, if TC-5619 achieves clinical proof of concept and AstraZeneca licenses TC-5619, our 2005 agreement with AstraZeneca provides for AstraZeneca to make a $40.0 million payment to us and to assume responsibility for and fund all future development and commercialization.

In that event, we would be eligible to receive additional payments of up to $226.0 million, contingent upon the achievement of development, regulatory, first commercial sale and first detail milestones for three indications, as well as stepped double-digit royalties on any future product sales.

As of December 31, 2009, we had received $45.0 million in aggregate payments under our alliance agreement with GlaxoSmithKline. These payments include a $20.0 million initial payment, the purchase of 1,275,502 shares of our common stock for an aggregate purchase price of $15.0 million, a $6.0 million payment upon our initiation of a Phase 1 clinical trial of a product candidate that had been in development for pain and $4.0 million in cumulative payments upon achievement of milestone events related to progress in our preclinical programs in therapeutic focus areas of the alliance. We are also eligible to receive other payments, contingent on the achievement of specified discovery, development, regulatory and commercial milestones in each therapeutic focus area of the alliance, as well as stepped double-digit royalties on any future sales of products licensed by GlaxoSmithKline.

Our 2009 agreement with AstraZeneca can be terminated by AstraZeneca in whole or in part at various times and under various circumstances as discussed above under the caption “Business—Strategic Collaborations—AstraZeneca AB—TC-5214—Termination” in Item 1 of Part I of this annual report. Our 2005 agreement with AstraZeneca can be terminated by AstraZeneca for an uncured material breach by us or upon 90 days notice given at any time, and our alliance agreement with GlaxoSmithKline can be terminated by GlaxoSmithKline for an uncured material breach by us or upon 90 days notice given at any time.

We acquired rights to Inversine, which is our only product to have been approved by the U.S. Food and Drug Administration, or FDA, for marketing, in August 2002. Effective September 30, 2009, we discontinued Inversine. Sales of Inversine generated net revenue of $473,000, $718,000 and $518,000 for the years ended December 31, 2009, 2008 and 2007, respectively.

From time to time we seek and are awarded grants or work to be performed under grants awarded to third-party collaborators from which we derive revenue. As of December 31, 2009 we have been awarded two grants from The Michael J. Fox Foundation for Parkinson’s Research, or MJFF. One of the grants is to fund research to test the potential of NNR Therapeutics to address Levodopa-induced abnormal involuntary movements, known as dyskinesias, and the other grant to fund research to identify NNR-related biomarkers relevant to Parkinson’s disease. Based on the terms of the awards, we expect to receive an aggregate of $641,000 over a one-year period that began in August 2009 in connection with the grant related to dyskinesias and an aggregate of $304,000 over a one-year period that began in December 2009 in connection with the grant related to biomarkers. In addition, as of December 31, 2009, we are a named subcontractor under a grant awarded to The California Institute of Technology by the National Institute on Drug Abuse, or NIDA, part of the National Institutes of Health, to fund research on innovative NNR-based approaches to the development of therapies for smoking cessation. We expect to receive approximately $1.1 million in the aggregate over a five-year period that began in July 2006 in connection with the NIDA grant. Funding for awards under federal grant programs is subject to the availability of funds as determined annually in the federal appropriations process.

Research and Development Expenses

Since our inception, we have focused our activities on our drug discovery and development programs. We record research and development expenses as they are incurred. Research and development expenses represented approximately 61%, 85% and 80% of our total operating expenses for the years ended December 31, 2009, 2008 and 2007, respectively. For 2009, license fees and royalties of $16.4 million, which are not included in research and development expenses, represented 25% of our total operating expenses. There were no license fees and royalties for the 2008 and 2007 periods.

Research and development expenses include costs associated with:

- the employment of personnel involved in our drug discovery, research and development activities;
- research and development facilities, equipment and supplies;

- clinical trials, including fees paid to contract research organizations to monitor and oversee some of our trials;
- costs to conduct research activities under the a4ß2 NNR research collaboration that we conducted with AstraZeneca from January 2006 to January 2010;
- the screening, identification and optimization of product candidates;
- formulation and chemical development;
- production of clinical trial materials, including fees paid to contract manufacturers;
- preclinical animal studies, including the costs to engage third-party research organizations;
- quality assurance activities;
- compliance with FDA regulatory requirements;
- consulting, license and sponsored research fees paid to third parties;
- the development and enhancement of our drug discovery technologies that we refer to as Pentad;
- depreciation of capital assets used to develop our products; and
- stock options granted to personnel in research and development functions.

We utilize our research and development personnel and infrastructure resources across several programs. We currently have clinical, preclinical and early research programs, and many of our costs are not specifically attributable to a single program. Instead, these costs are directed to broadly applicable research efforts. Accordingly, we cannot state precisely our total costs incurred on a program-by-program basis.

We have not received FDA or foreign regulatory marketing approval for any of our product candidates that are in development. Our current and future expenditures on preclinical and clinical development programs are subject to numerous uncertainties in timing and cost to completion. We test compounds in numerous preclinical studies for safety, toxicology and efficacy. We or a collaborator of ours then conducts clinical trials for those product candidates that are determined to be the most promising. If we do not establish an alliance or collaboration in which our collaborator assumes responsibility for funding the development of a particular product candidate, we fund these trials ourselves. As we or a collaborator of ours obtains results from clinical trials, we or the collaborator may elect to discontinue or delay trials for some product candidates in order to focus resources on more promising product candidates. Completion of clinical trials by us or a collaborator of ours may take several years or more, and the length of time generally varies substantially according to the type, complexity, novelty and intended use of a product candidate. The cost of clinical trials for a particular product candidate may vary significantly as a result of a variety of factors, including:

- the number of subjects who participate in the trials;
- the number and locations of sites included in the trials;
- the length of time required to enroll trial subjects;
- the therapeutic areas being investigated;
- the duration of the trials and subject follow-up;
- the costs of producing supplies of the product candidate needed for trials and regulatory submissions;
- the efficacy and safety profile of the product candidate; and
- the costs and timing of, and the ability to secure, regulatory approvals.

In addition, our strategy includes entering into alliances and collaborations with third parties to participate in the development and commercialization of some of our product candidates. Where a third party has responsibility

for or authority over any or all of the preclinical or clinical development of a particular product candidate, the estimated completion date may be largely under control of that third party and not under our control. We cannot forecast with any degree of certainty whether AstraZeneca will exercise any options to license particular product candidates that become exercisable under the terms of our 2005 agreement with AstraZeneca, whether GlaxoSmithKline will exercise any options to license particular product candidates that become exercisable under the terms of our alliance agreement with GlaxoSmithKline, whether any of our product candidates will be subject to future alliances or collaborations or how any such arrangements would affect our development plans or capital requirements. Because of this uncertainty, and because of the numerous uncertainties related to clinical trials and related activities as described above, we are unable to determine precisely the duration and completion costs of our research and development programs or whether or when we will generate revenue from the commercialization and sale of any of our product candidates in development.

General and Administrative Expenses

General and administrative expenses consist principally of salaries and other related costs for personnel in executive, finance, business development, legal and human resource functions. Other general and administrative expenses include expenses associated with stock options granted to personnel in those functions, depreciation and other facility costs not otherwise included in research and development expenses, patent-related costs, insurance costs and professional fees for consulting, legal, accounting and public and investor relations services.

License Fees and Royalties

License fees and royalties consist of amounts that we become required to pay to third parties from which we license or otherwise acquire intellectual property rights, such as University of South Florida Research Foundation, or USFRF, with respect to TC-5214 and University of Kentucky Research Foundation, or UKRF, with respect to AZD3480. Under the terms of a license agreement with USFRF, if we receive any milestone payments under our 2009 agreement with AstraZeneca, we would be required to pay a percentage of each such milestone payment, after deducting the unexhausted portion of our projected share of the costs of the initial development program for TC-5214, as well as royalties on any future product sales, to USFRF. The percentage of each milestone payment, net of any deduction, that we would be required to pay would be at least 10% and could be greater in specified circumstances. Based on the terms of the license agreement with USFRF and the terms of another license agreement with Yale University, we expect to pay royalties at an effective worldwide rate in the low single digits and such effective royalty rate could in some circumstances reach the mid single digits. Under the terms of a sponsored research agreement and a subsequent license agreement with UKRF, if we receive any milestone or royalty payments from AstraZeneca relating to AZD3480, we are required to pay a low single digit percentage of each such payment to UKRF.

The amount and timing of our payment obligations to USFRF depend on whether and when milestone events under our 2009 agreement with AstraZeneca are achieved and we receive the corresponding payments from AstraZeneca and whether and when regulatory approval for TC-5214 is obtained and product sales are generated. Likewise, the amount and timing of our payment obligations to UKRF depend on whether and when milestone events under our 2005 agreement with AstraZeneca are achieved and we receive the corresponding payments from AstraZeneca and whether and when regulatory approval for AZD3480 is obtained and product sales are generated. Accordingly, we cannot forecast with any degree of certainty whether or to what extent we will incur license fee and royalty expense in future periods.

Income Taxes

We have incurred cumulative net operating losses through 2009 and consequently have not paid federal, state or foreign income taxes for any period. As of December 31, 2009, we had net operating loss carryforwards of $155.7 million for federal income tax purposes and $138.9 million for state income tax purposes. We also had research and development income tax credit carryforwards of $7.4 million for federal income tax purposes and

$1.5 million for state income tax purposes as of December 31, 2009. The federal net operating loss carryforwards begin to expire in 2020. The state net operating loss carryforwards begin to expire in 2015. The federal and state research and development tax credits begin to expire in 2021. As a result of various factors, including the subjectivity of measurements used in the calculation of particular tax positions taken or that may in the future be taken in our tax returns and the uncertain statutory consequences of an administrative penalty of $5,600 that we were assessed in 2009 by the North Carolina Department of Environment and Natural Resources, it is uncertain whether or to what extent we will be eligible to use the tax credits for state income tax purposes.

Utilization of the net operating loss carryforwards and credits may be subject to a substantial annual limitation due to ownership change limitations provided by Section 382 of the Internal Revenue Code of 1986, as amended, and similar state provisions. When an ownership change, as defined by Section 382, occurs, an annual limitation is imposed on a company's use of net operating loss and credit carryforwards attributable to periods before the change. As a result of a series of stock issuances, we had such an ownership change in November 2002. Consequently, an annual limitation is imposed on our use of net operating loss and credit carryforwards that are attributable to periods before November 2002. In addition, a portion of the net operating loss carryforwards described above may potentially not be usable by us if we experience further ownership changes in the future. For financial reporting purposes, we have recorded a valuation allowance to fully offset the deferred tax assets related to the carryforwards and the tax credits because the likelihood that we will be eligible to use or realize any benefit from them is uncertain.

Fair Value

The carrying amounts of our cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses are considered to be representative of their respective fair values due to their short-term natures and, in the case of short-term investments, their market interest rates. Likewise, the carrying amount of our long-term debts are considered to be representative of their fair value due to their market interest rates. Our short-term investments in certificates of deposit of $27.0 million at December 31, 2009 are recorded at quoted market prices.

Our intangible assets consist of rights assigned to us from Layton Bioscience, Inc., including licensed patent rights and rights related to the Inversine trademark and product technology. Our original assigned value of the Inversine trademark and product technology intangible asset was $346,000. During the fourth quarter of 2008, as part of our processes for preparation of our financial statements, we performed an impairment analysis of the Inversine trademark and product technology intangible asset. As of the date of the analysis, we had recognized a net loss on sales of Inversine for each of 2008 and 2007 and did not expect to recognize net income from sales of Inversine in future periods. The history of losses on sales of Inversine and the forecast for future periods indicated the carrying value of the intangible asset may not have been recoverable. Using a discounted cash flow model that was based on estimated future net product sales and cost of product sales and considered assumptions such as, among other things, estimated future product sales volumes and estimated future sales price increases, we determined that the Inversine trademark and product technology had no fair value. As a result, we recorded an impairment charge for the full amount of the unamortized balance of the Inversine trademark and product technology intangible asset as of the valuation date, or $220,000, to research and development expenses in the fourth quarter of 2008. The impairment charge has no effect on our prospective amortization of the licensed patent rights intangible asset to research and development expenses on a straight-line basis over the remaining useful life of the patents.

Critical Accounting Policies and Estimates

Our management's discussion and analysis of our financial condition and results of operations are based on our financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, we evaluate these

estimates and judgments. We base our estimates on historical experience and on various assumptions that we believe to be reasonable under the circumstances. These estimates and assumptions form the basis for making judgments about the carrying values of assets and liabilities and the recording of revenues and expenses that are not readily apparent from other sources. Actual results and experiences may differ materially from these estimates. In addition, our reported financial condition and results of operations could vary if new accounting standards are enacted that are applicable to our business.

Our significant accounting policies are described in Note 2 to our audited financial statements for the year ended December 31, 2009 included in this annual report. We believe that our accounting policies relating to revenue recognition, accrued expenses and stock-based compensation are the most critical to understanding and evaluating our reported financial results. We have identified these policies as critical because they both are important to the presentation of our financial condition and results of operations and require us to make judgments and estimates on matters that are inherently uncertain and may change in future periods. For more information regarding these policies, you should refer to Note 2 to our audited financial statements included in this annual report.

Revenue Recognition

We derive a substantial portion of our revenues from our collaborations with AstraZeneca and our alliance with GlaxoSmithKline and expect that we will continue to derive a substantial portion of our revenues from these relationships over at least the next several years.

Our collaboration and alliance agreements contain multiple elements, including: upfront fees, which may include initial payments upon commencement of the contractual relationship, payment representing a common stock purchase premium or payment to secure a right for a future license; research fees for ongoing research and development; payments associated with the achievement of discovery, development, regulatory and commercial milestone events; and rights to receive royalties based on specified percentages of any net product sales. In determining the accounting for collaboration and alliance agreements, we first determine whether the agreement involves a single unit of accounting or separate units of accounting for revenue recognition purposes by evaluating each deliverable under the terms of the agreement. If a deliverable has value on a stand alone basis and there is objective and reliable evidence of that fair value, we treat the deliverable as a separate unit of accounting. If an agreement does not have multiple deliverables that meet these criteria, we consider the agreement to have one unit of accounting. If an agreement involves separate units of accounting, we then determine how to allocate amounts received under the agreement among the separate units, based on the respective fair value of each unit and the revenue recognition applicable to each unit. If an agreement involves a single unit of accounting, we determine the revenue recognition applicable to the entire agreement.

We defer recognition of non-refundable upfront fees and recognize them into revenue on a straight-line basis over (1) the estimated development period, to the extent the fees are attributable to a specific licensed product candidate, or otherwise (2) the estimated period of our performance obligations or where our collaborator has substantially all research and development responsibility, over the estimated research and development period. The period over which we recognize the revenue may be adjusted from time to time to take into account any delays or acceleration in the development of the applicable product candidate or any extension or shortening of the applicable performance period. Any such delay or acceleration in the development of a product candidate, or extension or shortening of a performance period, could result in further deferral of revenue or acceleration in the recognition of deferred revenue. As of December 31, 2009, all amounts that we have received from AstraZeneca and GlaxoSmithKline are non-refundable.

We recognize collaboration research and development revenue from research services performed under our collaboration agreements as research is performed and related expenses are incurred.

We recognize revenue for non-refundable payments that are based on the achievement of discovery, development, regulatory and commercial milestone events upon achievement of the milestone event if all of the following conditions are met:

- achievement of the milestone event was not reasonably assured at the inception of the arrangement;
- substantive effort is involved to achieve the milestone event; and
- the amount of the milestone payment appears reasonable in relation to the effort expended, the other milestone payments in the arrangement and the related risk associated with achievement of the milestone event.

If any of these conditions are not met, we would defer recognition of the payment and recognize the payment on a straight-line basis as discussed above.

To the extent we are reimbursed under a collaboration or alliance agreement for specific research and development costs, such as third-party manufacturing costs for drug material, we reflect these reimbursable amounts as a component of collaboration research and development revenue and we reflect the costs associated with these reimbursable amounts as a component of research and development expenses.

Under our 2009 agreement with AstraZeneca, we received an upfront payment of $200.0 million. We recorded such amount as deferred revenue and commenced recognizing the payment ratably over the estimated development period for TC-5214 in December 2009.

We have received various payments under our 2005 agreement with AstraZeneca.

- We received an initial fee of $10.0 million in February 2006. Based on the agreement terms and consideration of fair value, we allocated $5.0 million of the initial fee to the a4ß2 NNR research collaboration. Upon effectiveness of the agreement in January 2006, we commenced recognizing the $5.0 million as revenue over the planned four-year term of the research collaboration. We deferred recognition of the remaining $5.0 million of the initial fee, which we allocated to the AZD3480 license grants, until AstraZeneca made its determination in December 2006 to proceed with further development of AZD3480. Beginning in January 2007, we commenced recognizing the previously deferred $5.0 million of the initial fee ratably over the expected remaining development period for AZD3480.
- We received a $2.0 million payment from AstraZeneca in November 2007 to secure the right to license TC-5619 following our completion of an agreed development plan through a Phase 2 clinical proof of concept trial. Beginning in November 2007, we commenced recognizing the $2.0 million payment ratably over the expected development period to achieve clinical proof of concept.
- We have received cumulative research fees of $26.5 million since inception of the agreement. We recognized all of the research fees as the research was performed and related expenses were incurred.
- We have received payments from AstraZeneca upon achievement of milestone events related to the development of product candidates in the aggregate amount of $34.4 million since inception of the agreement. We recognized the full amount of each payment as revenue upon achievement of the corresponding milestone event because the event met each of the conditions required for immediate recognition under our revenue recognition policy.

We have also received various payments under our alliance agreement and related stock purchase agreement with GlaxoSmithKline.

- GlaxoSmithKline made an initial payment to us of $20.0 million and purchased 1,275,502 shares of our common stock for an aggregate purchase price of $15.0 million, which resulted in an aggregate deemed premium of $3.5 million based on the closing price of our common stock on the trading day

immediately preceding the date that the alliance was announced. In July 2007, we commenced recognizing the initial payment and deemed premium as revenue on a straight-line basis over the estimated term of our research and early development performance obligations under the agreement.

- In December 2007, we initiated a Phase 1 clinical trial of a product candidate that had been in development for pain, triggering a $6.0 million milestone payment to us from GlaxoSmithKline. We determined the milestone payment did not meet all of the conditions required for immediate revenue recognition. Specifically, based on the status of development of the product candidate as of the inception of the agreement, we determined that achievement of the milestone event was reasonably assured. Consequently, we recorded the $6.0 million payment as deferred revenue and, in December 2007, commenced recognizing such amount on a straight-line basis over the estimated term of our research and early development performance obligations under the agreement.
- We have received cumulative payments of $4.0 million from GlaxoSmithKline upon achievement of milestone events under the alliance agreement since the agreement's inception. We recognized the full amount of each payment as revenue upon achievement of the milestone event because the event met each of the conditions required for immediate recognition under our revenue recognition policy.

Accrued Expenses

In the normal course of our business, we contract with research institutions and contract research organizations that conduct or manage clinical trials or other research and development activities on our behalf and with contract manufacturers that produce drug substance or drug product for us. The financial terms of these agreements are subject to negotiation, vary from contract to contract and may result in uneven payment flows. Payments under these agreements depend on the performance of services or the achievement of specified events, such as the production of drug substance or drug product, the recruitment of clinical trial subjects, the completion of portions of a non-clinical study or clinical trial or similar conditions.

As part of the process of preparing financial statements, we are required to estimate accrued expenses with the objective of matching the recording of expenses in our financial statements to the actual services received and efforts expended. This process involves reviewing open contracts and purchase orders, communicating with our applicable personnel to identify services that have been performed on our behalf, estimating level of services performed and the associated cost incurred for the services when we have not yet been invoiced or otherwise notified of actual cost and reviewing invoices received that have not yet become due and payable. We make estimates of our accrued expenses as of each balance sheet date in our financial statements based on facts and circumstances known to us. We periodically confirm the accuracy of our estimates with the service providers and make adjustments if necessary. If we do not identify costs that we have begun to incur or if we underestimate or overestimate the level of services performed or the costs of these services, our actual expenses could differ from our estimates. Examples of estimated accrued expenses include:

- fees for services performed by contract research organizations in connection with preclinical studies and clinical trials;
- fees for services performed by clinical trial sites in connection with clinical trials;
- fees for services performed by contract manufacturers in connection with the production of clinical trial materials and, for the periods presented, Inversine; and
- professional service fees.

Stock-Based Compensation

We record the grant date fair value of stock options issued to employees and non-employee directors as stock-based compensation expense over the requisite service periods, which are typically the vesting periods. We currently use the Black-Scholes-Merton formula to estimate grant date fair value and expect to continue to use

this valuation model in the future. The Black-Scholes-Merton formula requires us to make various assumptions, including among others the expected term of the award and expected volatility of our common stock. We recorded stock-based compensation expense related to stock options granted to employees and directors of $2.4 million for the year ended December 31, 2009, $2.1 million for the year ended December 31, 2008 and $2.7 million for the year ended December 31, 2007. As of December 31, 2009, we had $2.9 million in total unrecognized compensation cost related to non-vested stock-based compensation arrangements, which we expect to record over a weighted average period of 2.6 years. On January 19, 2010, we granted to employees options to purchase an aggregate 841,072 shares of our common stock with an exercise price per share of $20.68. Recent market conditions may impact our assumptions that we use to estimate the grant date fair value of the awards using the Black-Scholes-Merton model. As a result, we have not yet finalized the estimate. We expect to record the aggregate fair value of these awards, after adjusting for forfeitures, as stock-based compensation expense on a straight line basis over a period of 16 quarters.

Results of Operations

Years ended December 31, 2009 and December 31, 2008

Net Operating Revenues

	Year ended December 31,		
	2009	2008	Change
		(in thousands)	
Operating revenues:			
Collaboration research and development	$ 5,246	$ 8,967	$(3,721)
Milestones and license fees from collaborations	18,934	10,179	8,755
Product sales, net	473	718	(245)
Grant revenue	409	221	188
Net operating revenues	$25,062	$20,085	$ 4,977

Net operating revenues for the year ended December 31, 2009 increased by $5.0 million as compared to the year ended December 31, 2008. The higher net operating revenues were primarily attributable to an increase of $8.8 million in milestones and license fees from collaborations, partially offset by a decrease of $3.7 million in collaboration research and development revenue. The increase in milestones and license fees from collaborations was principally attributable to a $10.0 million payment received under our 2005 agreement with AstraZeneca based on the achievement of the objective in the completed Phase 2 clinical trial of AZD3480 in adults with ADHD and recognition of $398,000 of the upfront payment received under our 2009 agreement with AstraZeneca. These increases were partially offset by a decrease of $1.0 million in payments received based on the achievement of preclinical milestone events under our 2005 agreement with AstraZeneca and our strategic alliance agreement with GlaxoSmithKline and our recognition of less deferred license fee revenue for 2009 as a result of an extension of the estimated development period for AZD3480 and an extension of the estimated development period for TC-5619 to reach Phase 2 clinical proof of concept.

The decrease in collaboration research and development revenue for the year ended December 31, 2009 reflected reduced services rendered by us in our preclinical research collaboration with AstraZeneca as a result of progress previously made toward meeting the objectives of the research plan. All of our collaboration research and development revenue for 2009 and 2008 was derived from our preclinical research collaboration with AstraZeneca. The preclinical research collaboration expired in January 2010 and, as a result, will not be a source of collaboration research and development revenue for future periods.

In future periods, we are eligible to receive additional license fees and milestone payments under our agreements with AstraZeneca and GlaxoSmithKline. The amount of license fees and milestone fees will depend on the timing and achievement of the discovery, development, regulatory and commercial milestone events,

whether AstraZeneca exercises its future right to license TC-5619 and whether GlaxoSmithKline exercises any options to license product candidates that arise under the agreement. The likelihood that we will achieve any particular milestone event in 2010, any future period or at all is uncertain. In particular, in February 2010, GlaxoSmithKline announced plans to cease discovery research in selected neuroscience areas, specifically including pain, which is one of the therapeutic focus areas of our alliance. Discussions with GlaxoSmithKline regarding the effects of its strategic change on our alliance are ongoing. Until these discussions are completed, the overall impact is uncertain, but we currently anticipate that multiple therapeutic focus areas in the alliance will be discontinued. In that event, we would no longer be eligible to receive contingent milestone payments from GlaxoSmithKline for those therapeutic focus areas. We expect that the amount of our milestone-based revenue may vary from period to period.

Net sales of Inversine for the year ended December 31, 2009 decreased by $245,000 as compared to the year ended December 31, 2008 primarily as a result of our discontinuation of Inversine effective as of September 30, 2009. Grant revenue for the year ended December 31, 2009 increased by $188,000 as compared to the year ended December 31, 2008. The higher grant revenue was primarily due to recognition of $147,000 of the amounts awarded by MJFF. We expect to recognize revenue of $798,000 for the remainder of the grants from MJFF during the year ending December 31, 2010.

Research and Development Expenses

	Year ended December 31,		
	2009	2008	Change
		(in thousands)	
Research and development expenses	$40,179	$40,981	$ (802)

Research and development expenses for the year ended December 31, 2009 decreased by $802,000 as compared to the year ended December 31, 2008. The lower research and development expenses were primarily attributable to a decrease of $908,000 in costs incurred for third-party research and development services in connection with our clinical-stage product candidates, including costs for clinical trial activities, formulation activities, production of clinical trial materials and pharmacology, toxicology and other non-clinical studies, to $10.3 million for 2009, from $11.2 million for 2008. This decrease in third-party research and development costs for our clinical-stage product candidates was partially offset by an increase of $310,000 in costs incurred for third-party research and development services in connection with our preclinical programs.

The costs that we incurred for the years ended December 31, 2009 and 2008 for third-party services in connection with research and development of clinical-stage product candidates are shown in the table below:

	Year ended December 31,		
	2009	2008	Change
		(in thousands)	
TC-5214	$ 5,527	$4,826	$ 701
TC-5619	2,585	3,151	(566)
TC-6987	1,752	78	1,674
AZD3480	217	322	(105)
AZD1446	—	—	—
	$10,081	$8,377	$1,704

The table above does not include costs incurred for TC-6499, a compound that we ceased developing in 2009 and for which we are now considering conducting an exploratory study in irritable bowel syndrome, or TC-2216. For the years ended December 31, 2009 and 2008, we incurred $221,000 and $2.8 million, respectively, in expenses for third-party research and development services in connection with these compounds.

We expect our research and development expenses for the year ending December 31, 2010 to increase, primarily as a result of our obligation under our 2009 agreement with AstraZeneca to fund a portion of the costs of Phase 3 clinical development of TC-5214.

General and Administrative Expenses

	Year ended December 31,		
	2009	2008	Change
	(in thousands)		
General and administrative expenses	$8,167	$6,499	$1,668

General and administrative expenses for the year ended December 31, 2009 increased by $1.7 million as compared to the year ended December 31, 2008. The higher general and administrative expenses were principally attributable to increased employee compensation and related expenses, primarily as a result of special bonuses paid to employees in December 2009, and increased legal and professional fees associated with our 2009 agreement with AstraZeneca.

License Fees and Royalties

	Year ended December 31,		
	2009	2008	Change
	(in thousands)		
License fees and royalties	$16,350	—	$ 16,350

License fees and royalties for the year ended December 31, 2009 increased by $16.4 million as compared to the year ended December 31, 2008. The higher license fees and royalties reflected $16.0 million payable to USFRF based on our receipt of the $200.0 million upfront payment under our 2009 agreement with AstraZeneca and $350,000 paid to UKRF based on the $10.0 million milestone payment received under our 2005 agreement with AstraZeneca based on the achievement of the objective in the completed Phase 2 clinical trial of AZD3480 in adults with ADHD.

Cost of Product Sales

	Year ended December 31,		
	2009	2008	Change
	(in thousands)		
Cost of product sales	$691	$749	$ (58)

Our cost of product sales are those costs related directly to the sale of Inversine. Cost of product sales for the year ended December 31, 2009 decreased by $58,000 as compared to the year ended December 31, 2008. The decrease was primarily attributable to our discontinuation of Inversine effective as of September 30, 2009.

Interest Income and Interest Expense

	Year ended December 31,		
	2009	2008	Change
	(in thousands)		
Interest income	$1,050	$2,734	$(1,684)
Interest expense	217	251	(34)

Interest income for the year ended December 31, 2009 decreased by $1.7 million as compared to the year ended December 31, 2008. The decrease was primarily attributable to lower short-term interest rates.

Interest expense for the year ended December 31, 2009 decreased by $34,000 as compared to the year ended December 31, 2008. The decrease was attributable to lower average principal balances under loan facilities used to finance equipment, furnishings, software and other fixed assets as we made scheduled payments.

Years ended December 31, 2008 and December 31, 2007

Net Operating Revenues

	Year ended December 31,		
	2008	2007	Change
	(in thousands)		
Operating revenues:			
Collaboration research and development	$ 8,967	$ 7,288	$1,679
Milestones and license fees from collaborations	10,179	3,548	6,631
Product sales, net	718	518	200
Grant revenue	221	222	(1)
Net operating revenues	$20,085	$11,576	$8,509

Net operating revenues for the year ended December 31, 2008 increased by $8.5 million as compared to the year ended December 31, 2007. The higher net operating revenues were principally attributable to an increase of $6.6 million in milestones and license fees from collaborations and to an increase of $1.7 million in collaboration research and development revenue. The increase in milestones and license fees from collaborations reflected $2.2 million in aggregate payments received from AstraZeneca upon the achievement of milestone events related to the progression of AZD1446 and $1.5 million in aggregate payments received from GlaxoSmithKline upon the achievement of milestone events related to progress in our smoking cessation and preclinical pain programs. The increase in milestones and license fees from collaborations also reflected recognition of an additional $2.9 million of deferred license fee revenue from payments received from GlaxoSmithKline and AstraZeneca in the second half of 2007 to $4.2 million for 2008, from $1.3 million for 2007. The increase in collaboration research and development revenue was primarily attributable to an increase of $2.0 million in research fees to $8.9 million for 2008, from $6.9 million for 2007, resulting from additional services rendered by us in the preclinical research collaboration that we conducted with AstraZeneca.

Net sales of Inversine for the year ended December 31, 2008 increased by $200,000 as compared to the year ended December 31, 2007. The increase resulted from a 62% increase in the sales price of Inversine made effective at the beginning of 2008, partially offset by a reduction in the volume of sales of Inversine. We instituted a 19% price increase for Inversine effective at the beginning of 2009.

Research and Development Expenses

	Year ended December 31,		
	2008	2007	Change
	(in thousands)		
Research and development expenses	$40,981	$34,620	$6,361

Research and development expenses for the year ended December 31, 2008 increased by $6.4 million as compared to the year ended December 31, 2007. The higher research and development expenses were principally attributable to an increase of $4.3 million in salary and benefit expenses and temporary personnel, supply and

infrastructure costs and an increase of $2.2 million in costs incurred for third-party preclinical research and development services. These increases resulted principally from greater activities in the therapeutic focus areas of our alliance with GlaxoSmithKline, which was formed in July 2007, and greater activities in the preclinical research collaboration that we conducted with AstraZeneca as product candidates progressed to later stages of research. A greater number of clinical-stage programs and progression of these programs during 2008 also contributed to the increase in salary and benefit expenses and temporary personnel, supply and infrastructure costs. These increases were partially offset by a decrease of $136,000 in costs incurred for third-party services in connection with research and development of clinical-stage product candidates, including costs for clinical trial activities, formulation activities, production of clinical trial materials and pharmacology, toxicology and other non-clinical studies, to $11.1 million for 2008, from $11.2 million for 2007. The costs that we incurred for the years ended December 31, 2008 and 2007 for third-party services in connection with research and development of clinical-stage product candidates are shown in the table below:

	Year ended December 31,		
	2008	2007	Change
	(in thousands)		
TC-5214	$ 4,826	$ 3,926	$ 900
TC-5619	3,151	2,937	214
TC-6499	2,291	1,566	725
TC-2216	549	1,687	(1,138)
AZD3480	322	—	322
	$11,139	$10,116	$ 1,023

In addition to the product candidates shown in the table above, we incurred expenses for third party-services in connection with TC-2696, a product candidate that we have since ceased developing, of $1.1 million for the year ended December 31, 2007. We did not incur any expenses in connection with the development of TC-2696 during 2008. The reported amount for TC-2216 for the year ended December 31, 2008 includes costs with respect to non-clinical studies conducted to characterize TC-2216 and its constituent enantiomers and costs with respect to our completed Phase 1 single rising dose clinical trial of TC-2216.

General and Administrative Expenses

	Year ended December 31,		
	2008	2007	Change
	(in thousands)		
General and administrative expenses	$6,499	$8,013	$(1,514)

General and administrative expenses for the year ended December 31, 2008 decreased by $1.5 million as compared to the year ended December 31, 2007. The lower general and administrative expenses were principally attributable to a decrease of $627,000 in employee bonuses and a decrease of $967,000 in stock-based compensation expense.

Cost of Product Sales

	Year ended December 31,		
	2008	2007	Change
	(in thousands)		
Cost of product sales	$749	$ 715	$ 34

Our cost of product sales are those costs related directly to the sale of Inversine. Cost of product sales for the year ended December 31, 2008 increased by $34,000 as compared to the year ended December 31, 2007. The increase was primarily attributable to an increase in product and establishment fees assessed by the FDA.

Interest Income and Interest Expense

	Year ended December 31,		
	2008	2007	Change
	(in thousands)		
Interest income	$2,734	$3,837	$(1,103)
Interest expense	251	138	113

Interest income for the year ended December 31, 2008 decreased by $1.1 million as compared to the year ended December 31, 2007. The decrease was primarily attributable to lower short-term interest rates.

Interest expense for the year ended December 31, 2008 increased by $113,000 as compared to the year ended December 31, 2007. The increase was attributable to higher average principal balances under loan facilities used to finance equipment, furnishings, software and other fixed assets. We borrowed $4.8 million under a loan agreement with a bank entered into in March 2008 and an additional $489,000 under the same loan facility in September 2008. We used $1.7 million of the proceeds from the March 2008 loan to refinance the principal and interest outstanding on two tranches of a previous loan facility.

Liquidity and Capital Resources

Sources of Liquidity

We have historically financed our operations and internal growth primarily through public and private offerings of our securities, payments under collaborations and alliances, including upfront fees, payments for research and development services and payments upon achievement of milestone events, equipment and building lease incentive financing, government grants and interest income. We discontinued our only approved product, Inversine, effective as of September 30, 2009. The net contribution from Inversine sales has not historically been a significant source of cash.

In December 2009, we entered into a collaboration and license agreement with AstraZeneca AB for the global development and commercialization of TC-5214. We received a $200.0 million upfront payment from AstraZeneca in January 2010.

In July 2007, we entered into a product development and commercialization agreement and related stock purchase agreement with GlaxoSmithKline. During 2009 and 2008, we received $4.0 million in cumulative payments from GlaxoSmithKline upon the achievement of milestone events related to progress in preclinical programs. As of December 31, 2009, we had received $45.0 million in aggregate payments from GlaxoSmithKline under the agreements.

In December 2005, we entered into a collaboration and license agreement with AstraZeneca. During 2009 and 2008, we received cumulative payments of $2.4 million from AstraZeneca upon achievement of milestone events related to the development of AZD1446 and another product candidate arising under the preclinical research collaboration that we conducted with AstraZeneca under the agreement. In July 2009, we received a $10.0 million payment from AstraZeneca as a result of the achievement of the objective in the completed Phase 2 trial of AZD3480 in adults with ADHD. As of December 31, 2009, we had received $44.4 million in aggregate upfront fees and milestone payments under the agreement and had recognized an additional $26.5 million in collaboration research and development revenue for research services that we provided in the preclinical research collaboration.

As discussed above under the caption “—Overview—Revenue,” we are eligible to receive substantial additional payments from AstraZeneca, contingent on the achievement of specified milestone events related to TC-5214, AZD3480, AZD1446, and TC-5619, if TC-5619 achieves clinical proof of concept and AstraZeneca

licenses it, and from GlaxoSmithKline, contingent on the achievement of specified milestone events in the specified therapeutic focus areas of the alliance. There is no assurance that we will achieve any particular milestone event in 2010, in any future period or at all. In particular, in February 2010, GlaxoSmithKline announced plans to cease discovery research in selected neuroscience areas. If GlaxoSmithKline's strategic change leads to the discontinuation of therapeutic focus areas of our alliance, we would no longer be eligible to receive contingent milestone payments from GlaxoSmithKline for those therapeutic focus areas, which would diminish the alliance as a potential source of future funds.

In October 2009 and January 2008, we completed public offerings of our common stock. The October 2009 offering consisted of 2.2 million shares at a price of $21.00 per share and, after deducting underwriting discounts and commissions and offering expenses payable by us, our net proceeds from the offering were $44.4 million. The January 2008 offering consisted of 4.4 million shares at a price of $7.07 per share and, after deducting underwriting discounts and commissions and offering expenses payable by us, our net proceeds from the offering were $29.1 million. Taken together with our initial public offering in April 2006, we have derived aggregate net proceeds of $114.3 million from public offerings of our common stock. We have also derived aggregate net proceeds of $121.8 million from private placements of convertible preferred stock, all of which occurred prior to our initial public offering.

In October 2009, we received written notice from a stockholder that the stockholder had violated Section 16(b) of the Exchange Act as a result of certain purchases and sales of shares of our common stock made by the stockholder within a period of less than six months that generated "short-swing" profits under Section 16(b). Later in October 2009, the stockholder made a $724,000 payment to us in disgorgement of the short-swing profits.

In March 2008, we entered into a loan agreement with a bank that provided borrowing capacity of $5.3 million to fund the purchase of equipment, furnishings, software and other fixed assets and enabled the refinancing of a previous loan facility that we had with R.J. Reynolds Tobacco Holdings, Inc., or RJRT. We borrowed $4.8 million upon entering into the loan agreement and borrowed the remaining $489,000 in September 2008. Pursuant to the loan agreement, we granted a first priority security interest in favor of the bank in the assets acquired with the proceeds of the loan facility. The March 2008 loan bears interest at a fixed rate of 5.231% per annum and is repayable in equal monthly installments of $112,000 beginning April 1, 2008 and continuing through the maturity date of March 1, 2012. We used $1.7 million of the proceeds from the March 2008 loan to pay and satisfy in full the principal and interest outstanding on two of the tranches under the loan facility with RJRT and granted a first priority security interest in favor of the bank in assets previously acquired with the proceeds of those tranches. The September 2008 loan bears interest at a fixed rate of 6.131% per annum and is repayable in equal monthly installments of $11,000 beginning October 1, 2008 and continuing through the maturity date of September 1, 2012. As of December 31, 2009, the outstanding principal balance under the loan facility was $3.2 million. There is no additional borrowing capacity remaining available to us under the loan agreement.

In April 2002, we received a $500,000 loan from the City of Winston-Salem. Under the terms of the loan, there was no interest accrual or payment due until the fifth anniversary of the loan. Following expiration of the five-year grace period in April 2007, the outstanding principal balance of the loan began to bear interest at an annual interest rate of 5% and became payable in 60 equal monthly installments of $9,000. As of December 31, 2009, the outstanding principal balance under the loan was $238,000.

Our cash, cash equivalents and short-term investments were $111.1 million as of December 31, 2009 and $88.4 million as of December 31, 2008. As of December 31, 2009, substantially all of our cash, cash equivalents and short-term investments were invested in bank depository accounts, certificates of deposit, and institutional money market funds at Branch Banking and Trust Company, RBC Bank and Wells Fargo & Company.

Cash Flows

	Year ended December 31,		
	2009	2008	Change
		(in thousands)	
Net cash used in operating activities	$(24,271)	$(28,261)	$ 3,990
Net cash provided by (used in) investing activities	9,800	(5,519)	15,319
Net cash provided by financing activities	47,178	31,579	15,599
Net increase (decrease) in cash and cash equivalents	$ 32,707	$ (2,201)	

	Year ended December 31,		
	2008	2007	Change
		(in thousands)	
Net cash (used in) provided by operating activities	$(28,261)	$ 24,838	$(53,099)
Net cash used in investing activities	(5,519)	(26,286)	20,767
Net cash provided by financing activities	31,579	13,107	18,472
Net (decrease) increase in cash and cash equivalents	$ (2,201)	$ 11,659	

Net cash used in operating activities for the year ended December 31, 2009 decreased by $4.0 million as compared to the year ended December 31, 2008. The decrease in net cash used in operating activities was primarily attributable to an increase in our accounts payable, license fees payable and accrued expenses of $16.5 million for 2009 as compared to a decrease of $1.9 million for 2008, a difference of $18.4 million. This difference was primarily due to the license fee payable at December 31, 2009 of $16.0 million based on the $200.0 million upfront payment receivable from AstraZeneca and was partially offset by an increase of $13.7 million in our net loss for 2009 to $39.4 million, from $25.7 million for 2008. We expect net cash used in operating activities for the year ended December 31, 2010 to increase, primarily as a result of our obligation under our 2009 agreement with AstraZeneca to fund a portion of the costs of Phase 3 clinical development of TC-5214.

Net cash used in operating activities was $28.3 million for the year ended December 31, 2008 and net cash provided by operating activities was $24.8 million for the year ended December 31, 2007, a change of $53.1 million. The change in net cash (used in) provided by operating activities was principally due to:

- a decrease in net loss of $2.4 million in 2008 to $25.7 million, from $28.1 million for the year ended December 31, 2007;
- a decrease in our collaboration revenue and accounts receivable balance of (1) $19.2 million for 2007 as a result of our receipt of a $20.0 million milestone payment from AstraZeneca in January 2007 triggered by achievement of a milestone event related to AZD3480 and (2) $2.1 million for 2008, a difference of $17.1 million;
- the addition in 2007 of an aggregate of $31.5 million in our deferred license fee revenue liability balance resulting from our receipt of a $20.0 million initial payment from GlaxoSmithKline and an aggregate deemed premium of $3.5 million resulting from GlaxoSmithKline's purchase of common stock, in each case in connection with the formation of our alliance in July 2007, our receipt of a $6.0 million milestone payment from GlaxoSmithKline upon our initiation of a Phase 1 clinical trial of a product candidate that had been in development for pain and our receipt of a $2.0 million payment from AstraZeneca to secure the future right to license TC-5619; and
- an increase of $2.9 million in deferred license fee revenue recognized for 2008, which includes $1.5 million greater recognition of the payments received from GlaxoSmithKline upon formation of our alliance, $635,000 greater recognition of the $6.0 million payment received from GlaxoSmithKline and $808,000 greater recognition of the payment received from AstraZeneca to secure the future right to license TC-5619.

Net cash provided by investing activities was $9.8 million for the year ended December 31, 2009 and net cash used in investing activities was $5.5 million for the year ended December 31, 2008, a change of $15.3 million. Net cash used in investing activities for the year ended December 31, 2008 decreased by $20.8 million as compared to the year ended December 31, 2007. Typically, cash provided by or used in investing activities reflects the portion of our cash that we allocate to, and the timing of purchases and maturities of, our investments. For example, a transfer of funds from a short-term investment to cash or a cash equivalent generates cash provided by investing activities, while a transfer of funds from cash or a cash equivalent to a short-term investment generates cash used in investing activities. During 2009, we re-allocated substantial funds from certificates of deposit to bank depository accounts and institutional money market funds as the certificates of deposit came due in order to yield more favorable interest rates. In addition to our investment activity, we purchased $200,000 of property and equipment for the year ended December 31, 2009, a decrease of $1.9 million from $2.1 million in property and equipment purchased for the year ended December 31, 2008. The $2.1 million of property and equipment for the year ended December 31, 2008 reflected a decrease of $2.8 million from $4.9 million in property and equipment purchases for the year ended December 31, 2007. Purchases of property and equipment for each of 2009, 2008 and 2007 were primarily for equipment required to support our research and development operations. The higher purchases in 2007 as compared to 2009 and 2008 were a result of furniture and equipment purchases in connection with the 2007 expansion of our leased facilities. We expect our net cash used in investing activities to increase significantly for the year ended December 31, 2010 as a result of the $200.0 million payment received from AstraZeneca in January 2010.

Net cash provided by financing activities for the year ended December 31, 2009 increased by $15.6 million as compared to the year ended December 31, 2008. The increase was primarily attributable to an increase of $19.2 million from net proceeds from issuance of common stock to $48.6 million for the year ended December 31, 2009, from $29.4 million for the year ended December 31, 2008, and was partially offset by a decrease in net borrowings of $3.6 million under our loan facilities for the year ended December 31, 2009 as compared to the year ended December 31, 2008. The net proceeds from issuance of common stock for the year ended December 31, 2009 reflected our receipt of $44.4 million in net proceeds from a public stock offering we completed in October 2009 and $3.4 million of proceeds upon exercise of stock options. The net proceeds from issuance of common stock for the year ended December 31, 2008 reflected our receipt of $29.1 million in net proceeds from a public stock offering that we completed in January 2008 and $271,000 of proceeds for the issuance of common stock upon exercise of stock options.

Net cash provided by financing activities for the year ended December 31, 2008 increased by $18.5 million as compared to the year ended December 31, 2007. The increase was principally attributable to our receipt of $29.1 million in net proceeds from our January 2008 public stock offering and incremental net borrowings of $1.0 million under our loan facilities for the year ended December 31, 2008, partially offset by our receipt of $11.5 million, net of the deemed premium, from GlaxoSmithKline for the purchase of common stock in July 2007.

Funding Requirements

As of December 31, 2009, we had an accumulated deficit of $229.3 million. We expect to incur operating losses for the foreseeable future. Our future capital requirements are difficult to forecast and will depend on many factors, including:

- whether and to what extent milestone events are achieved for TC-5214 under our December 2009 agreement with AstraZeneca and for AZD3480 and AZD1446 under our December 2005 agreement with AstraZeneca;
- the progress of, and outcomes from, Phase 3 clinical development of TC-5214 and the amount and timing of development costs for TC-5214 payable by us;
- whether, following our completion of our ongoing Phase 2 clinical trial of TC-5619 in cognitive dysfunction in schizophrenia, AstraZeneca exercises its right to license TC-5619;

- the scope, progress, duration, results and cost of clinical trials, as well as non-clinical studies and assessments, of our other product candidates;
- whether and to what extent research and development-related milestone events are achieved under our alliance agreement with GlaxoSmithKline;
- the extent to which we retain development and commercialization rights or responsibilities for our product candidates that are not subject to our collaborations with AstraZeneca or our alliance with GlaxoSmithKline and incur associated development costs, manufacturing costs or costs to establish sales and marketing functions;
- whether we establish strategic alliances, collaborations and licensing or other arrangements on terms favorable to us;
- the costs, timing and outcomes of regulatory reviews or other regulatory actions;
- the number and characteristics of product candidates that we pursue;
- the costs of preparing, filing and prosecuting patent applications and maintaining, enforcing and defending intellectual property-related claims;
- the costs of manufacturing-related services for our product candidates in clinical and late preclinical development;
- the rate of technological advancements for the indications that we target;
- the costs to satisfy our obligations under existing and potential future alliances and collaborations;
- the timing, receipt and amount of sales or royalties, if any, from our potential products; and
- the extent and scope of our general and administrative expenses.

Implementing our strategy may require additional capital as our clinical-stage and preclinical product candidates advance into later-stage development, as we progress our programs, invest in additional product opportunities and expand our research and development infrastructure. Our existing capital resources may not be sufficient to enable us to fund the completion of the development of any of our product candidates. We currently expect our existing capital resources to be sufficient to fund our operations at least through the end of 2013, without taking into account amounts that we would be entitled to receive if milestone events are achieved under either of our agreements with AstraZeneca or our agreement with GlaxoSmithKline. However, our operating plan may change as a result of many factors, including those described above, and we may need additional funds sooner than planned to meet operational needs and capital requirements for product development.

We do not expect to generate sufficient cash from our operations to sustain our business for the foreseeable future. To the extent our capital resources are insufficient to meet future capital requirements, we may need to finance future cash needs through alliances, collaborations or licensing arrangements, public or private equity or debt offerings or other financings. The global credit and financial markets continue to be negatively impacted by the recessionary environment. This, coupled with other factors, may dramatically limit our access to additional equity or debt financing in the future on acceptable terms or at all. Also, additional strategic alliances, collaborations or licensing arrangements may not be available on acceptable terms or at all. If adequate funds are not available, we may be required to delay, reduce the scope of or eliminate our research and development programs or obtain funds through arrangements with collaborators or others that may require us to relinquish rights to certain product candidates that we might otherwise seek to develop or commercialize independently. Additionally, any future equity funding may dilute the ownership of our stockholders.

We cannot accurately determine the completion dates and related costs of our research and development programs due to inherent uncertainties in outcomes of clinical trials and regulatory approvals of our product candidates. We cannot be certain that we will be able to successfully complete our research and development

projects or establish strategic alliances, collaborations or licensing or other arrangements for our product candidates. The failure of us or any of our collaborators to complete research and development programs for our product candidates could have a material adverse effect on our financial position or results of operations.

To date, inflation has not had a material effect on our business.

Contractual Obligations

The following table summarizes our fixed contractual obligations as of December 31, 2009:

	Payments Due by Period				
Contractual Obligation	Total	Less Than 1 Year	1-3 Years	3-5 Years	More Than 5 Years
			(in thousands)		
Long-term debt obligations	$ 3,630	$ 1,590	$2,040	$—	$ —
Operating lease obligations	5,578	2,159	3,419	—	—
License fee obligations	16,070	16,070	—	—	—
Purchase obligations	7,051	7,016	34	1	—
	$32,329	$ 26,835	$5,493	$ 1	$ —

The license fee obligation in the above table reflects the amount payable to USFRF based on our receipt of the $200.0 million upfront payment under our 2009 agreement with AstraZeneca. The amounts of license fee obligations for all periods reflected in the above table exclude contingent license and royalty payments that we may become required to make under our technology license agreements and other contingent payments that we may become required to make under our technology license agreements upon achievement of specified development, regulatory or commercial milestones. The amounts of purchase obligations reflected in the above table include obligations to purchase drug product or drug substance, to compensate clinical investigators, clinical trial sites and contract research organizations contingent on the performance of services in connection with clinical trials and to compensate contract research organizations contingent on the performance of non-clinical research and development services, but do not include our share of the anticipated development costs for TC-5214. The amounts of purchase obligations also include contractual obligations for insurance and other general and administrative expenses.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board issued Accounting Standards Update No. 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements—a consensus of the FASB Emerging Issues Task Force*, or ASU 2009-13. ASU 2009-13 addresses the units of accounting for arrangements involving multiple deliverables and how arrangement consideration should be allocated to the separate units of accounting, when applicable. ASU 2009-13 eliminates the criterion in prior accounting guidance that objective and reliable evidence of the fair value of any undelivered items must exist for the delivered items to be considered a separate unit or separate units of accounting. ASU 2009-13 is effective for financial statements issued for fiscal years beginning after June 15, 2010 and can be applied either prospectively or retrospectively for all periods presented. We are in the process of determining the impact of ASU 2009-13 on our financial results.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

The primary objective of our investment activities is to preserve our capital to fund operations. We also seek to maximize income from our investments without assuming significant risk. To achieve our objectives, we maintain a portfolio of cash equivalents and investments in a variety of securities that are considered to be high credit quality. Our investments are typically short-term in nature. As of December 31, 2009, we had cash, cash equivalents and short-term investments of $111.1 million. Our investments may be subject to interest rate risk and could fall in value if market interest rates increase. However, because our investments are short term in duration, we believe that our exposure to interest rate risk is not significant and estimate that an immediate and uniform 10% increase in market interest rates from levels as of December 31, 2009 would not have a material impact on the total fair value of our portfolio.

We contract for the conduct of some of our clinical trials and other research and development and manufacturing activities with contract research organizations, clinical trial sites and contract manufacturers in Europe and India. We may be subject to exposure to fluctuations in foreign currency exchange rates in connection with these agreements. If the average Euro/U.S. dollar or Indian Rupee/U.S. dollar exchange rate were to strengthen or weaken by 10% against the corresponding exchange rate as of December 31, 2009, we estimate that the impact on our financial position, results of operations and cash flows would not be material. We do not hedge our foreign currency exposures.

We have not used derivative financial instruments for speculation or trading purposes.

Item 8. Financial Statements and Supplementary Data.

INDEX TO THE FINANCIAL STATEMENTS

TARGACEPT, INC.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of
Targacept, Inc.

We have audited the accompanying balance sheets of Targacept, Inc. as of December 31, 2009 and 2008, and the related statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Targacept, Inc. at December 31, 2009 and 2008, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2009, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Targacept, Inc.'s internal control over financial reporting as of December 31, 2009, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 11, 2010 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Raleigh, North Carolina
March 11, 2010

TARGACEPT, INC.

BALANCE SHEETS
(in thousands, except share and par value amounts)

	December 31, 2009	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 83,909	$ 51,202
Short-term investments	27,157	37,161
Receivables from collaborations and trade accounts	201,801	2,073
Prepaid expenses and inventories	1,562	1,530
Total current assets	314,429	91,966
Property and equipment, net	4,783	6,401
Intangible assets, net of accumulated amortization of $129 and $112 at December 31, 2009 and 2008, respectively	167	184
Total assets	$ 319,379	$ 98,551
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 1,275	$ 1,500
License fee payable	16,000	—
Accrued expenses	5,158	4,381
Current portion of long-term debt	1,442	1,390
Current portion of deferred rent incentive	42	42
Current portion of deferred license fee revenue	77,243	6,479
Total current liabilities	101,160	13,792
Long-term debt, net of current portion	1,966	3,408
Deferred rent incentive, net of current portion	67	109
Deferred license fee revenue, net of current portion	147,195	23,869
Total liabilities	250,388	41,178
Commitments and contingencies		
Stockholders' equity:		
Common stock, $0.001 par value, 100,000,000 shares authorized at December 31, 2009 and December 31, 2008, and 28,226,829 and 24,964,373 shares issued and outstanding at December 31, 2009 and December 31 2008, respectively	28	25
Capital in excess of par value	298,263	247,244
Accumulated deficit	(229,300)	(189,896)
Total stockholders' equity	68,991	57,373
Total liabilities and stockholders' equity	$ 319,379	$ 98,551

See accompanying notes.

TARGACEPT, INC.

STATEMENTS OF OPERATIONS
(in thousands, except share and per share amounts)

	Year ended December 31,		
	2009	2008	2007
Operating revenues:			
Collaboration research and development	$ 5,246	$ 8,967	$ 7,288
Milestones and license fees from collaborations	18,934	10,179	3,548
Product sales, net	473	718	518
Grant revenue	409	221	222
Net operating revenues	25,062	20,085	11,576
Operating expenses:			
Research and development (including stock-based compensation of $1,353, $1,130 and $845 in 2009, 2008 and 2007, respectively)	40,179	40,981	34,620
General and administrative (including stock-based compensation of $1,101, $935 and $1,902 in 2009, 2008 and 2007, respectively)	8,167	6,499	8,013
License fees and royalties	16,350	—	—
Cost of product sales	691	749	715
Total operating expenses	65,387	48,229	43,348
Loss from operations	(40,325)	(28,144)	(31,772)
Other income (expense):			
Interest income	1,050	2,734	3,837
Interest expense	(217)	(251)	(138)
Total other income (expense)	833	2,483	3,699
Loss before income taxes	(39,492)	(25,661)	(28,073)
Income tax benefit	88	—	—
Net loss	$ (39,404)	$ (25,661)	$ (28,073)
Basic and diluted net loss per share	$ (1.54)	$ (1.04)	$ (1.42)
Weighted average common shares outstanding—basic and diluted	25,636,419	24,664,169	19,720,732

See accompanying notes.

TARGACEPT, INC.

STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except share amounts)

	Common Stock		Capital in Excess of Par Value	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount			
Balances at December 31, 2006	19,132,233	$ 19	$201,142	$ (136,162)	$ 64,999
Issuance of common stock related to exercise of stock options	95,684	—	432	—	432
Stock-based compensation	—	—	2,747	—	2,747
Net proceeds from sale of common stock to GlaxoSmithKline	1,275,502	1	11,478	—	11,479
Net loss and comprehensive loss	—	—	—	(28,073)	(28,073)
Balances at December 31, 2007	20,503,419	$ 20	$215,799	$ (164,235)	$ 51,584
Issuance of common stock related to exercise of stock options	90,954	—	271	—	271
Stock-based compensation	—	—	2,065	—	2,065
Net proceeds from public stock offering	4,370,000	5	29,109	—	29,114
Net loss and comprehensive loss	—	—	—	(25,661)	(25,661)
Balances at December 31, 2008	24,964,373	$ 25	$247,244	$ (189,896)	$ 57,373
Issuance of common stock related to exercise of stock options	1,062,456	1	3,353	—	3,354
Stock-based compensation	—	—	2,454	—	2,454
Net proceeds from public stock offering	2,200,000	2	44,447	—	44,449
Stockholder short swing profit payment	—	—	724	—	724
Federal income tax benefit	—	—	41	—	41
Net loss and comprehensive loss	—	—	—	(39,404)	(39,404)
Balances at December 31, 2009	28,226,829	$ 28	$298,263	$ (229,300)	$ 68,991

See accompanying notes.

TARGACEPT, INC.

STATEMENTS OF CASH FLOWS
(in thousands)

	Year ended December 31,		
	2009	2008	2007
Operating activities			
Net loss	$(39,404)	$ (25,661)	$ (28,073)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:			
Depreciation and amortization	1,835	1,800	907
Recognition of deferred license fee revenue	(6,383)	(6,479)	(3,548)
Impairment of intangible asset	—	220	—
Stock-based compensation expense	2,454	2,065	2,747
Changes in operating assets and liabilities:			
Receivables from collaborations and trade accounts(1)	272	2,125	19,171
Prepaid expenses, inventories and accrued interest receivable	(28)	(413)	270
Accounts payable, license fees payable and accrued expenses	16,510	(1,918)	1,843
Deferred license fee revenue(1)	473	—	31,521
Net cash (used in) provided by operating activities	(24,271)	(28,261)	24,838
Investing activities			
Purchase of investments	(31,000)	(104,800)	(151,751)
Proceeds from sale of investments	41,000	101,334	130,409
Purchase of property and equipment	(200)	(2,053)	(4,944)
Net cash provided by (used in) investing activities	9,800	(5,519)	(26,286)
Financing activities			
Proceeds from issuance of long-term debt	—	5,300	2,000
Principal payments on long-term debt	(1,390)	(3,106)	(805)
Proceeds from issuance of common stock, net	48,568	29,385	11,912
Net cash provided by financing activities	47,178	31,579	13,107
Net increase (decrease) in cash and cash equivalents	32,707	(2,201)	11,659
Cash and cash equivalents at beginning of year	51,202	53,403	41,744
Cash and cash equivalents at end of year	$ 83,909	$ 51,202	$ 53,403

(1) Exclusive of $200,000 non-cash item related to the Company's December 2009 collaboration and license agreement with AstraZeneca AB (see Note 13).

See accompanying notes.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2009

1. The Company and Nature of Operations

Targacept, Inc., a Delaware corporation (the Company), was formed on March 7, 1997. The Company is a biopharmaceutical company engaged in the design, discovery and development of novel NNR Therapeutics™ for the treatment of diseases and disorders of the central nervous system. The Company's NNR Therapeutics selectively target neuronal nicotinic receptors, or NNRs. Its facilities are located in Winston-Salem, North Carolina.

2. Summary of Significant Accounting Policies

Use of Estimates and Reclassifications

The preparation of financial statements in conformity with U.S. generally accepted accounting principles, or GAAP, requires management to make estimates and assumptions that affect the amounts of assets, liabilities, revenues and expenses reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

Certain reclassifications have been made to the financial statements for the year ended December 31, 2008 to conform to the presentation in the financial statements for the year ended December 31, 2009. These reclassifications had no impact on previously reported net loss.

Cash and Cash Equivalents

The Company considers cash equivalents to be those investments which are highly liquid, readily convertible to cash and mature within three months from the date of purchase.

Short-Term Investments

Consistent with the Company's investment policy, cash is invested with established financial institutions in bank depository accounts, certificates of deposit, and institutional money market funds. The Company determines the appropriate classification of marketable securities at the time of purchase and reevaluates the designation as of each balance sheet date. All marketable securities owned during 2009 and 2008 were classified as available for sale. Interest and dividend income on investments are included in "Interest income." The cost of securities sold is based on the specific identification method.

Through July 2008, the Company had also invested surplus cash in student loan auction rate securities, or ARS. In June and July 2008, all of the Company's student loan ARS were redeemed by the issuers of the underlying securities at full par value. The Company has not held investments in student loan ARS since July 2008.

Receivables from Collaborations and Trade Accounts

Substantially all of the Company's collaboration revenue is related to the collaboration and alliance agreements discussed in Note 13. Substantially all of the Company's receivables from collaborations and trade accounts at December 31, 2009 are related to the Company's collaboration agreement with AstraZeneca AB entered into in December 2009 (see Note 13). The Company's receivables from collaborations and trade accounts at December 31, 2008 are related to the collaboration and alliance agreements discussed in Note 13 and also include accounts receivable from trade sales of the Company's approved product Inversine. All of the Company's trade accounts receivable are due from customers located within the United States.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

2. Summary of Significant Accounting Policies—(continued)

The Company makes judgments with respect to the collectability of trade accounts receivable based on historical experience and current economic trends. Actual collections could differ from those estimates. The Company discontinued Inversine effective September 30, 2009.

During 2009, 2008 and 2007, the Company recognized revenue of $24,180,000, $19,146,000, and $10,836,000, respectively, or 96%, 95% and 94% of net operating revenues, respectively, from the collaboration and alliance agreements discussed in Note 13.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined by the weighted average method and consists of materials and manufacturing costs.

Property and Equipment and Intangible Assets

Property and equipment consists primarily of laboratory equipment, office furniture and fixtures and leasehold improvements and is recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets ranging from 3-10 years. Laboratory equipment is typically depreciated over 3-5 years, office furniture and fixtures are typically depreciated over 5-10 years, and leasehold improvements are typically amortized over the lesser of the asset life or the lease term.

Intangible assets consist of rights assigned by Layton Bioscience, Inc. The remaining intangible assets are being amortized to research and development expense on a straight-line basis over the useful life of the patents to which a license was assigned, a period of 17 years from the date of acquisition.

The Company assesses the net realizable value of its long-lived assets and evaluates these assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment charge would be recognized when estimated undiscounted future cash flows expected to result from the use of the asset and its eventual disposition are less than its carrying amount. An impairment charge, if recognized, would be based on the excess of the carrying value of the impaired asset over its estimated fair value.

Patents

The Company capitalizes the costs of patents purchased from external sources as intangible assets. The Company expenses all other patent-related costs.

Research and Development Expense

Research and development costs are expensed as incurred and include salaries of, and stock-based compensation for, personnel involved in research and development activities, contractor fees, administrative expenses and allocations of research-related overhead costs. Administrative expenses and research-related overhead costs included in research and development expense consist of allocations of facility and equipment lease charges, depreciation and amortization of assets, and insurance, legal and supply costs that are directly related to research and development activities. The Company directly reduces research and development expenses for amounts reimbursed pursuant to the cost-sharing agreements described in Note 13.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

2. Summary of Significant Accounting Policies—(continued)

Accrued Expenses

The Company records accruals based on estimates of the services received, efforts expended and amounts owed pursuant to contracts with clinical trial sites, contract research organizations and other service providers. In the normal course of business, the Company contracts with third parties to perform various clinical trial and other research and development activities in the ongoing development of potential products. The financial terms of these agreements are subject to negotiation, vary from contract to contract and may result in uneven payment flows. Payments under these agreements depend on the performance of services or the achievement of specified events, such as the production of drug substance or drug product, the recruitment of clinical trial subjects, the completion of portions of a non-clinical study or clinical trial or similar conditions. The objective of the Company's accrual policy is to match the recording of expenses in its financial statements to the actual services received and efforts expended. As such, expense accruals are recognized based on the Company's estimate of the degree of completion of the event or events specified in a particular contract as giving rise to a payment.

Deferred Rent Incentive

In August 2002, the Company received $2,013,000 as an incentive to lease its current facility. Through December 31, 2006, the incentive was recognized on a straight-line basis over the initial five-year term of the lease as a reduction to the lease expense. In January 2007, the Company renewed its lease for its current facility through July 2012 and began recognizing the remaining incentive over the renewal term. The Company recognized $42,000 of the incentive during each of 2009, 2008 and 2007.

Fair Value of Financial Instruments

The carrying amounts of cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses are considered to be representative of their respective fair values due to their short-term natures and, in the case of short-term investments, their market interest rates. Likewise, the carrying amounts of our long-term debts are considered to be representative of their fair value due to their respective market interest rates.

Credit Risk

Financial instruments that potentially subject the Company to credit risk consist principally of cash, short-term investments and receivables from collaborations and trade accounts. The Company has established guidelines for investment of its cash that are designed to emphasize safety, liquidity and preservation of capital. The Company places its cash and cash equivalents with established financial institutions. At December 31, 2009 and 2008, the Company had deposits in excess of federally insured limits of $110,159,000 and $87,452,000, respectively.

Revenue Recognition

The Company uses the revenue recognition guidance established by Financial Accounting Standards Board, or FASB, Accounting Standards Codification, or ASC, Topic 605, *Revenue Recognition*, or ASC 605. In determining the accounting for collaboration and alliance agreements, the Company follows the provisions of Subtopic 25 of ASC 605, *Multiple Element Arrangements*, or ASC 605-25. ASC 605-25 provides guidance on whether an arrangement that involves multiple revenue-generating activities or deliverables should be divided

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

2. Summary of Significant Accounting Policies—(continued)

into separate units of accounting for revenue recognition purposes and, if a division is required, how the arrangement consideration should be allocated among the separate units of accounting. If the arrangement constitutes separate units of accounting according to the separation criteria of ASC 605-25, a revenue recognition policy must be determined for each unit. If the arrangement constitutes a single unit of accounting, the revenue recognition policy must be determined for the entire arrangement.

Collaboration research and development revenue is earned and recognized as research is performed and related expenses are incurred. Non-refundable upfront fees, which may include an initial payment upon commencement of the contractual relationship, payment representing a common stock purchase premium or payment to secure a right for a future license, are recorded as deferred licensed fee revenue and recognized into revenue as milestone and license fees from collaborations on a straight-line basis over (1) the estimated development period, to the extent the fees are attributable to a specific licensed product candidate, or otherwise (2) the estimated period of the Company's performance obligations or, where the Company's collaborator has substantially all research and development responsibility, over the estimated research and development period.

Revenue for non-refundable payments based on the achievement of collaboration milestones is recognized as revenue when the milestones are achieved if all of the following conditions are met: (1) achievement of the milestone event was not reasonably assured at the inception of the arrangement; (2) substantive effort is involved to achieve the milestone event; and (3) the amount of the milestone payment appears reasonable in relation to the effort expended, the other milestone payments in the arrangement and the related risk associated with achievement of the milestone event. If any of these conditions is not met, the milestone payment is deferred and recognized on a straight-line basis as discussed above.

Revenues for specific research and development costs that are reimbursable under collaboration agreements are recognized in accordance with ASC 605, Subtopic 45, *Principal Agent Considerations*. The revenue associated with these reimbursable amounts is reflected as a component of collaboration research and development revenue and the costs associated with these reimbursable amounts is reflected as a component of research and development expense.

Product sales revenue is recorded when goods are shipped, at which point title has passed, net of allowances for returns and discounts. Revenue from a grant is recognized as the Company performs the work and incurs reimbursable costs in accordance with the objectives of the award. Grant payments received prior to the Company's performance of work required by the terms of the award are recorded as deferred revenue and recognized as grant revenue as the Company performs the work and incurs qualifying costs.

Shipping and Handling Costs

During 2009, 2008 and 2007, cost of product sales included $183,000, $204,000, and $215,000 of shipping and handling costs, respectively.

Income Taxes

The Company uses the liability method in accounting for income taxes as required by ASC Topic 740, *Income Taxes*, or ASC 740. Under ASC 740, deferred tax assets and liabilities are recognized for operating loss and tax credit carryforwards and for the future tax consequences attributable to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

2. Summary of Significant Accounting Policies—(continued)

assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in the results of operations in the period that includes the enactment date. A valuation allowance is recorded to reduce the carrying amounts of deferred tax assets unless it is more likely than not that these assets will be realized. ASC 740 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. ASC 740 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods and disclosures. The Company's policy is to classify any interest recognized in accordance with ASC 740 as interest expense and to classify any penalties recognized in accordance with ASC 740 as an expense other than income tax expense.

Net Loss Per Share

The Company computes net loss per share in accordance with ASC Topic 260, *Earnings Per Share*, or ASC 260. Under the provisions of ASC 260, basic net loss per share, or Basic EPS, is computed by dividing net loss by the weighted average number of common shares outstanding. Diluted net loss per share, or Diluted EPS, is computed by dividing net loss by the weighted average number of common shares and dilutive common share equivalents outstanding. Common share equivalents consist of the incremental common shares issuable upon the exercise of stock options. For the periods presented, the Company has excluded all common share equivalents from the calculation of net loss per share because their effect is antidilutive. As a result, historical Diluted EPS is identical to historical Basic EPS for the periods presented.

For each of 2009, 2008 and 2007, shares subject to dilutive outstanding stock options may have been included in the calculation of common share equivalents using the treasury stock method if the Company had been in a net income position for such period. Shares subject to potentially dilutive outstanding stock options totaled 3,648,268 for 2009, 3,123,249 for 2008 and 2,628,087 for 2007, in each case calculated on a weighted-average basis.

Public Offerings of Common Stock

On April 18, 2006, the Company completed an initial public offering, or IPO, of 5,000,000 shares of its common stock at a price of $9.00 per share. The Company's net proceeds from the IPO, after deducting underwriters' discounts and commissions and offering expenses payable by the Company, were $40,775,000. The Company's common stock began trading on the NASDAQ Global Market (formerly known as the NASDAQ National Market) on April 12, 2006.

On January 23, 2008, the Company completed a public offering of 4,370,000 shares of its common stock at a price of $7.07 per share. The Company's net proceeds from the offering, after deducting underwriters' discounts and commissions and offering expenses payable by the Company, were $29,114,000.

On October 13, 2009, the Company completed a public offering of 2,200,000 shares of its common stock. The offering was priced to the public at $21.00 per share. The Company's net proceeds from the offering, after deducting underwriters' discounts and commissions and offering expenses payable by the Company, were $44,449,000.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

2. Summary of Significant Accounting Policies—(continued)

In October 2009, the Company was notified by one of its stockholders that the stockholder had generated short swing profits under the provisions of Section 16(b) of the Exchange Act on its purchases and sales of shares of the Company's common stock. The amount of realized profit under Section 16(b) was calculated to be $724,000, and the stockholder made a payment to the Company in that amount later in October.

Stock-Based Compensation

The Company has two stock-based incentive plans, the 2000 Equity Incentive Plan of Targacept, Inc., as amended and restated through March 15, 2006, or the 2000 Plan, and the Targacept, Inc. 2006 Stock Incentive Plan, as amended and restated through November 28, 2007 and further amended effective June 10, 2009, or the 2006 Plan. The 2000 Plan and the 2006 Plan, or the Plans, are described more fully in Note 10.

The Company records stock-based compensation under the fair value recognition provisions of ASC Topic 718, *Compensation—Stock Compensation*, or ASC 718. Under ASC 718, the Company calculates the fair value of each option grant using the Black-Scholes-Merton valuation formula. The fair value of each grant is recorded as expense on a straight-line basis over the option's vesting period.

ASC 718 also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow. This requirement reduces net operating cash flows and increases net financing cash flows for periods after adoption. The Company recognized $41,000 in excess tax deductions during 2009. The Company cannot estimate the future effect of excess tax deductions or shortfalls on cash flows because they depend on, among other things, when employees exercise stock options and the tax deductions available to the Company at those times. No financing or operating cash flows have been recognized in periods prior to 2009 for excess tax deductions because of cumulative net operating losses generated since inception and because the related deferred tax assets are offset by a valuation allowance.

Non-refundable Advance Payments

The Company defers and capitalizes non-refundable advance payments for goods or services to be received in the future for use in research and development activities. The Company then charges the advance payments to expense ratably as the goods are delivered or the services are rendered in accordance with ASC Subtopic 730-20, *Research and Development Arrangements*, or ASC 730-20. If the Company's expectations change such that it does not expect it will need the goods to be delivered or the services to be rendered, it will charge the remaining balance of capitalized non-refundable advance payments to expense. The provisions of ASC 730-20 became effective on January 1, 2008, and the Company adopted ASC 730-20 as of that date. Application of the provisions of ASC 730-20 resulted in an increase in total assets of $701,000 and a decrease in net loss of $273,000, or $0.01 per share, for the year ended December 31, 2009 and an increase in total assets and a decrease in net loss of $428,000, or $0.02 per share, for the year ended December 31, 2008.

Fair Value Accounting

Effective January 1, 2008, the Company adopted ASC Topic 820, *Fair Value Measurements and Disclosures*, or ASC 820, for application to financial assets. ASC 820 defines fair value, provides a consistent framework for measuring fair value under GAAP and expands fair value financial statement disclosure requirements. ASC 820 does not require any new fair value measurements, but applies only to accounting standards that already require or permit fair value measures (except for standards that relate to share-based payments such as ASC Topic 718, *Compensation—Stock Compensation*).

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

2. Summary of Significant Accounting Policies—(continued)

The valuation techniques of ASC 820 are based on both observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, and unobservable inputs reflect the Company's market assumptions. ASC 820 classifies these inputs into the following hierarchy:

Level 1 Inputs—Quoted prices for identical instruments in active markets.

Level 2 Inputs—Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs—Primarily unobservable value drivers.

As of December 31, 2009, the Company had $27,157,000 in available-for-sale marketable securities, comprised entirely of certificates of deposit and the related accrued interest receivable. The Company determines fair value for certificates of deposit through quoted market prices, or Level 1 inputs. The adoption of ASC 820 had no effect on the valuation of the Company's available-for-sale marketable securities as of December 31, 2009 or December 31, 2008.

The Company valued non-financial assets as of December 31, 2008, such as intangible assets measured at fair value for an impairment assessment (see Note 6), using other accounting standards in accordance with Section 15, *Scope and Scope Exceptions*, of ASC 820, Subtopic 10, *Overall*.

Comprehensive Loss

For each of the years ended December 31, 2009, 2008, and 2007, the Company's comprehensive loss equaled its reported net loss.

Recent Accounting Pronouncements

In October 2009, the FASB issued Accounting Standards Update No. 2009-13, *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements—a consensus of the FASB Emerging Issues Task Force*, or ASU 2009-13. ASU 2009-13 addresses the units of accounting for arrangements involving multiple deliverables and how arrangement consideration should be allocated to the separate units of accounting, when applicable. ASU 2009-13 eliminates the criterion in prior accounting guidance that objective and reliable evidence of the fair value of any undelivered items must exist for the delivered items to be considered a separate unit or separate units of accounting. ASU 2009-13 is effective for financial statements issued for fiscal years beginning after June 15, 2010 and can be applied either prospectively or retrospectively for all periods presented. The Company is in the process of determining the impact of ASU 2009-13 on its financial results.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

3. Short-term Investments

As of the respective dates shown, the Company's short-term investments consisted of:

	December 31, 2009	December 31, 2008
	(in thousands)	
Certificates of deposit	$ 27,000	$ 37,000
Accrued interest	157	161
	$ 27,157	$ 37,161

4. Inventories

As of the respective dates shown, inventories consisted of the following:

	December 31, 2009	December 31, 2008
	(in thousands)	
Raw materials	$—	$ 52
Finished goods	—	48
	$—	$100

Effective as of September 30, 2009, the Company discontinued its product Inversine. As a result, the Company recorded aggregate charges of $77,000 related to the impairment of its remaining raw materials and finished goods inventory to cost of product sales for the year ended December 31, 2009. The discontinuation of Inversine did not have a material impact on the Company's cash flows or results of operations for any of the periods presented, and the Company does not expect the discontinuation of Inversine to have a material impact on its cash flows or results of operations for future periods.

5. Property and Equipment

As of the respective dates shown, property and equipment consisted of the following:

	December 31, 2009	December 31, 2008
	(in thousands)	
Laboratory equipment	$ 10,371	$10,268
Office furniture and fixtures	3,328	3,232
Leasehold improvements	1,133	1,133
	14,832	14,633
Less: accumulated depreciation	(10,049)	(8,232)
Property and equipment, net	$ 4,783	$ 6,401

The Company recorded $1,818,000, $1,767,000, and $869,000 of depreciation expense for the years ended December 31, 2009, 2008 and 2007, respectively.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

6. Intangible Assets

As of the respective dates shown, intangible assets consisted of the following:

	December 31, 2009	December 31, 2008
	(in thousands)	
Patents	$ 296	$ 296
Less: accumulated amortization	(129)	(112)
Total	$ 167	$ 184

Intangible assets consist of rights assigned by Layton Bioscience, Inc. in 2002, which include licensed patent rights and rights related to the Inversine trademark and product technology. The licensed patent rights intangible asset had an original value to the Company of $296,000, and the Inversine trademark and product technology intangible asset had an original value to the Company of $346,000. During the fourth quarter of 2008, as part of its processes for preparation of its financial statements, the Company performed an impairment analysis of its intangible assets. As of the date of the analysis, the Company had recognized a net loss on sales of Inversine in each of 2008 and 2007 and did not expect to recognize net income from sales of Inversine in future periods. The history of losses on sales of Inversine and the forecast for future periods indicated the carrying value of the Inversine trademark and product technology intangible asset may not have been recoverable. Using a discounted cash flow model that is based on estimated future net product sales and cost of product sales and considers assumptions such as, among other things, estimated future product sales volumes and estimated future sales price increases, the Company estimated the fair value of the Inversine trademark and product technology intangible asset and determined that it had no fair value. As a result, the Company recorded an impairment charge for the full amount of the unamortized balance of the Inversine trademark and product technology intangible asset as of the valuation date, or $220,000, to research and development expense in the fourth quarter of 2008. The impairment charge had no effect on the Company's prospective amortization of the licensed patent rights intangible asset to research and development expense on a straight-line basis over the remaining useful life of the patents.

The Company recorded amortization expense of $17,000, $33,000, and $38,000 during the years ended December 31, 2009, 2008, and 2007, respectively, and expects to recognize $17,000 of amortization expense for each of the next five years.

7. Accrued Expenses

As of the respective dates shown, accrued expenses consisted of the following:

	December 31, 2009	December 31, 2008
	(in thousands)	
Clinical and preclinical trial costs	$ 2,551	$ 2,618
Employee compensation	2,447	1,484
Other	160	279
Total	$ 5,158	$ 4,381

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

8. Long-term Debt

During 2002, the Company borrowed $500,000 from the City of Winston-Salem. The note payable to the City of Winston-Salem matures on April 19, 2012 and was non-interest bearing until April 2007 when it began to bear interest at an annual rate of 5% or 7%, depending on the gross revenue of the Company. No payments were due on the City of Winston-Salem note until April 2007, when the Company began making monthly payments of $9,000 on the loan based on an interest rate of 5%.

In March 2008, the Company entered into a loan agreement with a bank that provided borrowing capacity of $5,300,000 to fund the purchase of equipment, furnishings, software and other fixed assets and enable the refinancing of an existing loan facility with another lender. The Company borrowed $4,811,000 upon entering into the loan agreement and borrowed the remaining $489,000 in September 2008. The Company's March 2008 loan bears interest at a fixed rate of 5.231% per annum and is repayable in equal monthly installments of $112,000 beginning April 1, 2008 through the maturity date of March 1, 2012. The Company used $1,679,000 of the proceeds from the March 2008 loan to pay and satisfy in full the principal and interest outstanding on two tranches of the existing loan facility with another lender and granted a first priority security interest in favor of the bank in assets previously acquired with the proceeds of those tranches. The Company's September 2008 loan bears interest at a fixed rate of 6.131% per annum and is repayable in equal monthly installments of $11,000 beginning October 1, 2008 through the maturity date of September 1, 2012.

The Company paid $223,000, $244,000 and $128,000 in interest under notes payable during the years ended December 31, 2009, 2008 and 2007, respectively. Maturities of long-term debt were as follows at December 31, 2009 (in thousands):

2010	$1,442
2011	1,521
2012	445
2013 and thereafter	—
	$3,408

9. Income Taxes

For the year ended December 31, 2009, the Company recognized an $88,000 income tax benefit primarily as a result of elections to forgo certain "bonus depreciation" deductions for federal income tax purposes in exchange for refundable research and development tax credits under the Housing Assistance Tax Act of 2008, as extended by the American Recovery and Reinvestment Act of 2009. For each of the years ended December 31, 2008 and 2007, there was no provision (benefit) for federal or state income taxes because the Company incurred net operating losses. The Company has incurred cumulative net operating losses since inception.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

9. Income Taxes—(continued)

The Company's effective tax rate differs from the federal income tax rate for the following reasons:

	Year Ended December 31,		
	2009	2008	2007
Expected federal income tax benefit/expense at statutory rate	35%	34%	34%
Increase (decrease) resulting from:			
Research and development credits	5	4	3
Stock-based compensation	(1)	(1)	(1)
State income tax expense, net of federal benefit	4	4	4
Change in valuation allowance	(41)	(41)	(40)
Other	(2)	—	—
	— %	— %	— %

At December 31, 2009, 2008 and 2007, the Company had net operating loss carryforwards for federal income tax purposes of $155,702,000, $113,648,000 and $113,093,000, respectively, and for state income tax purposes of $138,864,000, $113,493,000 and $113,083,000, respectively. At December 31, 2009, 2008 and 2007, the Company had research and development income tax credits for federal income tax purposes of $7,403,000, $6,118,000 and $3,910,000, respectively. The Company had research and development income tax credits for state income tax purposes of $1,488,000 at December 31, 2009. The Company's eligibility to use these research and development income tax credits in the future is uncertain. The federal net operating loss carryforwards begin to expire in 2020. The state net operating loss carryforwards begin to expire in 2015. The federal and state research and development tax credits begin to expire in 2021.

Utilization of the net operating loss carryforwards and credits may be subject to a substantial annual limitation due to ownership change limitations provided by Section 382 of the Internal Revenue Code of 1986, as amended, and similar state provisions. As a result of a series of stock issuances, the Company had such an ownership change on November 30, 2002. Consequently, an annual limitation is imposed on the Company's use of net operating loss and credit carryforwards attributable to periods before the change.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company's net deferred tax assets relate principally to its net operating loss carryforwards and recognition of deferred license fees from collaborations. A valuation allowance has been recognized to offset the deferred tax assets. If and when recognized, the tax benefit for those items will be reflected in current operations of the period in which the benefit is recorded as a reduction of income tax expense. The utilization of the loss carryforwards to reduce future income taxes will depend on the Company's ability to generate sufficient taxable income prior to the expiration of the net operating loss carryforwards. For the years ended December 31, 2009, 2008 and 2007, the valuation allowance increased $16,181,000, $10,574,000 and $10,619,000, respectively.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

9. Income Taxes—(continued)

As of the respective dates shown, significant components of the Company's deferred tax assets (liabilities) were as follows:

	December 31,	
	2009	2008
	(in thousands)	
Deferred tax assets:		
Net operating loss carryforward	$ 50,750	$ 40,951
Research and development tax credit	6,346	4,240
Collaboration revenue	9,296	11,701
Accrued royalties	6,068	—
Patents	1,704	1,605
Stock-based compensation	1,317	1,129
Total gross deferred tax assets	75,481	59,626
Valuation allowance	(75,311)	(59,130)
Net deferred tax asset	170	496
Deferred tax liabilities		
Equipment and other	(170)	(496)
Net deferrred tax asset	$ —	$ —

For the year ended December 31, 2009, stock option exercises resulted in $5,716,000 in excess tax deductions. The benefit of these excess tax deductions had not begun to be realized as of December 31, 2009 because the Company has incurred cumulative net operating losses. Accordingly, the tax benefit will not be recognized as an increase to capital in excess of par value until the excess deductions reduce income taxes payable.

The Company follows the provisions ASC 740, which prescribes a threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods and disclosures. There was no cumulative effect adjustment upon adoption.

A reconciliation of beginning and ending unrecognized tax benefits is as follows (in thousands):

Balance at January 1, 2007	$ 720
Additions based on tax positions related to the current year	222
Balance at December 31, 2007	942
Additions based on tax positions related to the current year	278
Balance at December 31, 2008	1,220
Additions based on tax positions related to the current year	532
Additions based on tax positions related to prior years	134
Balance at December 31, 2009	$ 1,886

Because of the impact of deferred tax accounting, none of the unrecognized tax benefits would, if recognized, affect the effective tax rate. No interest or penalties with respect to unrecognized tax positions are

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

9. Income Taxes—(continued)

recognized in the statement of operations for any of the years ended December 31, 2009, 2008 or 2007. The Company believes it is reasonably possible that unrecognized tax benefits may increase in the range of $200,000 to $300,000 during 2010, primarily as a result of additional research and development credits that the Company may become able to claim.

Since the Company has incurred cumulative net operating losses since inception, all tax years remain open to examination by major jurisdictions. An examination of the Company's 2006 federal income tax return was completed in 2009 with no adjustments. The Company's 2007, 2006 and 2005 North Carolina tax returns are under examination.

10. Stock-Based Incentive Plans

On August 22, 2000, the Company established the 2000 Plan to attract and retain employees, directors and certain independent contractors, consultants and advisors and to allow them to participate in the growth of the Company. The 2006 Plan became effective in April 2006 and is the successor equity incentive program to the 2000 Plan. All shares previously reserved under the 2000 Plan and not subject to outstanding awards under the 2000 Plan are now reserved for grant under the 2006 Plan. As of December 31, 2009, the number of shares authorized for issuance under the Plans was 7,282,078, of which 3,181,775 shares remained available for grant.

Awards may be made with respect to the 2006 Plan, or may have been made with respect to both Plans, to participants under the Plans in the form of incentive and nonqualified stock options, restricted stock, stock appreciation rights, stock awards, and performance awards. Eligible participants under the Plans include employees, directors and certain independent contractors, consultants or advisors of the Company or a related corporation. Awards made under the Plans have vesting periods that are determined at the discretion of the administrator and range from 0 to 5 years and most commonly have 10-year contractual terms or, in some cases, shorter terms designed to comply with Section 409A of the Internal Revenue Code. The exercise price of incentive options granted under the Plans may not be less than 100% of the fair market value of the common stock on the date of grant, as determined by the administrator.

Under ASC 718, the Company recognizes the grant date fair value of stock options issued to employees and non-employee directors over the requisite service periods, which are typically the vesting periods. The Company uses the Black-Scholes-Merton formula to estimate the fair value of its stock-based payments. The volatility assumption used in the Black-Scholes-Merton formula is based on the calculated historical volatility of twelve to sixteen benchmark companies in the Company's industry that have been identified as comparable public entities. The expected term for stock options granted during 2009, 2008 and 2007 is based on historical analysis. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

The following table illustrates the weighted average assumptions for the Black-Scholes-Merton model used in determining the fair value of stock options granted as of the respective dates shown:

	Year ended December 31,		
	2009	2008	2007
Dividend yield	—	—	—
Risk-free interest rate	2.0%	3.4%	4.0%
Volatility	0.7	0.7	0.7
Expected term	6.72 years	6.43 years	6.55 years

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

10. Stock-Based Incentive Plans—(continued)

A summary of option activity and changes during each of the years ended December 31, 2009, 2008 and 2007 appears below:

	Shares Subject to Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2006	2,476,977	$ 3.89		
Granted	789,386	8.83		
Forfeited	(45,518)	4.75		
Exercised	(95,684)	4.52		
Outstanding at December 31, 2007	3,125,161	5.11		
Granted	106,485	6.71		
Forfeited	(21,595)	6.73		
Exercised	(90,954)	2.98		
Outstanding at December 31, 2008	3,119,097	5.21		
Granted	779,400	3.06		
Forfeited	(12,229)	4.30		
Exercised	(1,062,456)	3.16		
Outstanding at December 31, 2009	2,823,812	$ 5.40	7.03	$ 43,781
Vested and exercisable at December 31, 2009	1,887,486	$ 5.76	6.28	$ 28,574

The weighted average grant date fair value of options granted during the years ended December 31, 2009, 2008, and 2007 was $2.03, $4.38, and $6.02, respectively. The total intrinsic value of options exercised during the years ended December 31, 2009, 2008, and 2007 was $16,833,000, $489,000, and $461,000, respectively.

A summary of the status of non-vested stock options granted under the 2006 Plan as of December 31, 2009 and changes during the year ended December 31, 2009 appears below:

	Shares Subject to Options	Weighted Average Grant-Date Fair Value Per Share
Non-vested at January 1, 2009	783,719	$ 4.76
Granted	779,400	2.03
Vested	(615,356)	3.80
Forfeited	(11,437)	2.75
Non-vested at December 31, 2009	936,326	$ 3.14

As of December 31, 2009, there was $2,937,000 of total unrecognized compensation cost related to non-vested stock-based compensation arrangements granted under the Plans, before considering estimated forfeitures. That cost is expected to be recorded over a weighted average period of 2.55 years. The total fair value of shares subject to stock-based compensation arrangements granted under the Plans that vested during the years ended December 31, 2009, 2008, and 2007 was $2,338,000, $2,217,000 and $2,612,000, respectively. On

10. Stock-Based Incentive Plans—(continued)

January 19, 2010, the compensation committee of the Company's board of directors granted to the Company's employees options to purchase an aggregate of 841,072 shares of the Company's common stock at an exercise price per share of $20.68. Recent market conditions may impact the assumptions used by the Company to estimate the grant date fair value of the awards using the Black-Scholes-Merton model. As a result, the Company has not yet finalized the estimate. The Company expects to record the aggregate fair value of the awards, after adjusting for forfeitures, as stock-based compensation on a straight-line basis over a period of 16 quarters.

The Company had 2,823,812 and 3,119,097 shares of common stock reserved for future issuance upon the exercise of outstanding stock options at December 31, 2009 and 2008, respectively.

11. Commitments and Contingencies

Operating Lease

On March 1, 2002, the Company entered into an agreement with Wake Forest University Health Sciences to lease an office and research facility in Winston-Salem, North Carolina with an initial term that extended through July 31, 2007. The lease contained a renewal option for up to one additional five-year term, with a rental rate for the renewal term similar to the initial term. From 2005 to 2007, the terms of the lease were amended to, among other things, include an additional approximately 18,400 square feet in the aggregate, provide the Company with an option to lease additional space in the facility and include a second renewal term, exercisable at the Company's option, at the then-existing market rate for similar space in the Piedmont Triad in North Carolina. The Company exercised its first renewal option in January 2007 and, as a result, the lease extends until July 31, 2012.

Rent expense incurred by the Company under the lease was $2,159,000 for each of the years ended December 31, 2009 and 2008, and $2,176,000 for the year ended December 31, 2007. Rent expense is partially offset by the monthly recognition of the deferred rent incentive discussed in Note 2.

The following table illustrates expected future lease payments under the lease (in thousands):

2010	$2,159
2011	2,159
2012	1,260
2013 and thereafter	—
	$5,578

Employment Arrangements

The Company has entered into employment agreements with its executive officers. Under the agreements, if the Company terminates the employment of the executive officer other than for just cause or if the executive officer terminates his employment for good reason, in each case as that term is defined in the agreement, the executive officer is entitled, among other things, to receive severance equal to his current base salary for nine to twelve months following termination or, if shorter, until he secures other employment. The executive officer would also be entitled to continuation of the health and life insurance benefits coverage provided to him as of the date of termination for the period during which he receives severance.

12. Retirement Savings Plan

The Company has a 401(k) retirement plan in which all of its employees are eligible to participate. The Company contributed $666,000, $558,000, and $559,000 to the plan for the years ended December 31, 2009, 2008 and 2007, respectively.

13. Strategic Alliance and Collaboration Agreements

AstraZeneca AB

December 2005 – Cognitive Disorders

In December 2005, the Company entered into a collaborative research and license agreement with AstraZeneca AB under which the Company granted AstraZeneca exclusive development and worldwide commercialization rights to the Company's product candidate known as AZD3480 (TC-1734) as a treatment for specified conditions characterized by cognitive impairment, including attention deficit/hyperactivity disorder, or ADHD. The Company is eligible to receive license fees and milestone payments under the agreement. The amount of license fees and milestone payments depends on the timing and achievement of development, regulatory, first commercial sale and first detail milestone events.

AstraZeneca paid the Company an initial fee of $10,000,000 in February 2006. Based on the agreement terms, the Company allocated $5,000,000 of the initial fee to the research collaboration, which the Company recognized as revenue on a straight-line basis over the four-year term of the research collaboration. The Company deferred recognition of the remaining $5,000,000 of the initial fee, which was allocated to the AZD3480 license grants, until December 2006, when AstraZeneca made a determination to proceed with further development of AZD3480 following the completion of additional clinical and non-clinical studies that AstraZeneca conducted during 2006. On December 27, 2006, AstraZeneca communicated its decision to proceed with further development of AZD3480 to the Company. As a result, in the first quarter of 2007, the Company began recognizing the $5,000,000 of the initial fee that it had previously deferred as revenue on a straight-line basis over the then-estimated five-year development period for AZD3480. In July 2009, the Company announced that it had been informed by AstraZeneca of AstraZeneca's plans to conduct further development of AZD3480 for ADHD. The Company extended its estimate of the development period for AZD3480 to continue through 2013 and began recognizing the portion of the $5,000,000 initial fee not yet recognized as of April 1, 2009 as revenue on a straight–line basis over the remaining estimated development period. The Company recognized $1,934,000 of the initial fee as revenue for the year ended December 31, 2009 and $2,250,000 of the initial fee as revenue for each of the years ended December 31, 2008 and 2007.

Under the agreement, the Company is also eligible to receive (1) additional payments of up to $103,000,000 if development, regulatory, and first commercial sale milestones for AZD3480 are achieved only for ADHD, (2) other payments if development, regulatory, first commercial sale and first detail milestones for AZD3480 are achieved for any other target indication under the agreement and (3) if regulatory approval is achieved for AZD3480 for any particular indication, stepped double-digit royalties on any sales of AZD3480 for that indication or any other indication. Under the terms of a sponsored research agreement and a subsequent license agreement between the Company and University of Kentucky Research Foundation, or UKRF, if the Company receives any of these payments from AstraZeneca relating to AZD3480, including royalties, the Company is required to pay a low-single digit percentage of each such payment to UKRF.

With respect to AZD1446, the most advanced product candidate that arose out of the parties' preclinical research collaboration described below, the Company is also eligible to receive payments of up to $108,000,000,

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

13. Strategic Alliance and Collaboration Agreements—(continued)

contingent upon the achievement of development, regulatory, first commercial sale and first detail milestone events for AZD1446 for two target indications under the agreement, and, if regulatory approval is achieved for AZD3480 for any particular indication, stepped royalties on any sales of AZD1446 for that indication or any other indication.

The Company would recognize any revenue based on the achievement of milestones under the agreement upon achievement of the milestone event if the Company determines that the revenue satisfies the requirements for immediate recognition under its revenue recognition policy (see Note 2).

The Company and AstraZeneca also conducted a multi-year preclinical research collaboration under the agreement. The term of the research collaboration expired in January 2010. While the research collaboration was ongoing, the Company was eligible to receive payments from AstraZeneca for research services performed. The Company recognized collaboration research and development revenue as the research was performed and related expenses were incurred. The Company recognized collaboration research and development revenue of $5,246,000, $8,921,000 and $6,888,000 for the years ended December 31, 2009, 2008 and 2007, respectively. The Company recognized additional collaboration research and development revenue of $46,000 and $400,000 for the years ended December 31, 2008 and 2007, respectively, for clinical trial material purchased by AstraZeneca from the Company and other research and development costs reimbursable under the collaboration.

In October 2007, the Company provided notice under its agreement with AstraZeneca offering AstraZeneca the right to license its product candidate TC-5619 for specified conditions characterized by cognitive impairment. Based on a subsequent election by AstraZeneca made under the terms of the agreement, AstraZeneca paid the Company $2,000,000 and the Company agreed to develop TC-5619 independently through completion of Phase 1 clinical development and a Phase 2 clinical proof of concept clinical trial in accordance with a mutually acceptable development plan, following which AstraZeneca would have the right to license TC-5619 on terms specified in the agreement. The Company is recognizing the $2,000,000 payment as revenue on a straight-line basis over the expected development period for TC-5619 to reach Phase 2 proof of concept. Accordingly, the Company recognized $596,000, $923,000 and $115,000 of the payment as revenue for the years ended December 31, 2009, 2008 and 2007, respectively.

In July 2009, the Company received from AstraZeneca a $10,000,000 payment based on achievement of the objective in a completed Phase 2 clinical trial of AZD3480 in adults with ADHD, a milestone event under an amendment to its agreement. The Company also received payments from AstraZeneca of $2,000,000 in December 2008 and $200,000 in May 2008, in each case based on achievement of a milestone event related to the development of AZD1446, and of $200,000 in June 2009 based on the achievement of a milestone event related to the development of another product candidate arising under the parties' preclinical research collaboration. The Company recognized the full amount of each of the payments described in this paragraph as revenue upon achievement of the corresponding milestone event because the event met each of the conditions required for immediate recognition under its revenue recognition policy (see Note 2). In December 2009, the Company made a payment of $350,000 to UKRF as a result of the $10,000,000 payment received from AstraZeneca described above.

AstraZeneca has paid the Company an aggregate of $70,920,000 under the December 2005 agreement since its inception.

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

13. Strategic Alliance and Collaboration Agreements—(continued)

December 2009 – TC-5214

In December 2009, the Company entered into a collaboration and license agreement with AstraZeneca AB for the global development and commercialization of TC-5214. Under the agreement, AstraZeneca made an upfront payment to the Company of $200,000,000 and the Company is eligible to receive cumulative payments of up to an additional $540,000,000 if specified development, regulatory and first commercial sale milestones are achieved, cumulative payments of up to an additional $500,000,000 if specified sales related milestones are achieved and significant stepped double-digit royalties on net sales worldwide. The Company recorded the upfront payment made by AstraZeneca as deferred license fee revenue and is recognizing the payment as revenue on a straight-line basis over the estimated development period for TC-5214 to submission of a new drug application to the U.S. Food and Drug Administration. The Company forecasts the new drug application submission date to be September 30, 2012. The Company recognized $398,000 of the upfront payment as revenue in 2009. The Company would recognize any revenue based on the achievement of milestones under the agreement upon achievement of the milestone event if the Company determines that the revenue satisfies the requirements for immediate recognition under its revenue recognition policy (see Note 2).

The Company and AstraZeneca have jointly designed a program for the global development of TC-5214. The initial clinical program is planned to include development of TC-5214 as an adjunct therapy and as a second-line “switch” monotherapy, in each case in adults with major depressive disorder who do not respond adequately to first-line antidepressant treatment. AstraZeneca is responsible for 80% of the cost of the initial program, except that AstraZeneca is responsible for 100% of development costs that are required only to obtain or maintain regulatory approval in countries outside the United States and the European Union. The Company is responsible for 20% of the costs of the initial program but has the right to terminate its obligation to fund its share of these costs once it has funded a specified amount. If the Company funds the specified amount and terminates its obligation to fund its share of further costs of the initial development program, any future milestones and royalties payable to the Company under this agreement would be reduced by the amount of the Company’s unfunded share plus interest, subject to a maximum reduction that may be applied to any one payment. In addition, if the Company and AstraZeneca mutually agree to develop TC-5214 for any indication other than major depressive disorder or in any formulation other than those contemplated by the initial program, the same cost sharing arrangement would apply, except that the Company would have the immediate right to terminate its obligation to fund its share of development costs for the other indication or formulation. If the Company terminates its obligation to fund its share of these other development costs, any future milestones and royalties payable to the Company under this agreement would be reduced by the amount of the Company’s unfunded share plus interest, subject to a maximum reduction that may be applied to any one payment, but only from and after the occurrence of a specified event to be agreed upon by the parties.

AstraZeneca is responsible under the agreement for executing and funding the costs of global commercialization of TC-5214. The Company has retained an option to co-promote TC-5214 to a specified target physician audience in the United States. If the Company exercises its co-promotion option, AstraZeneca would compensate the Company on a per detail basis. AstraZeneca is also responsible under the agreement for the manufacture and supply of TC-5214.

Under the terms of an existing license agreement, the Company is required to pay to University of South Florida Research Foundation, or USFRF, $16,000,000 based on the Company’s receipt of the upfront payment from AstraZeneca and would be required to pay to USFRF a percentage of each milestone payment that may be received from AstraZeneca, after deducting from such payment the unexhausted portion of the Company’s

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

13. Strategic Alliance and Collaboration Agreements—(continued)

projected share of the costs of the initial development program for TC-5214, as well as royalties on any future product sales. The percentage of each milestone payment, net of any deduction, that the Company would be required to pay would be at least 10% and could be greater in specified circumstances. Based on the terms of the license agreement with USFRF and the terms of another existing license agreement with Yale University, the Company expects to pay royalties at an effective worldwide rate in the low single digits and such effective royalty rate could in some circumstances reach the mid single digits. As of December 31, 2009, the Company has accrued a license fee payable to USFRF of $16,000,000.

GlaxoSmithKline

On July 27, 2007, the Company entered into a product development and commercialization agreement with SmithKline Beecham Corporation, doing business as GlaxoSmithKline, and Glaxo Group Limited, which are referred to together as GlaxoSmithKline, that sets forth the terms of an alliance designed to discover, develop and market product candidates that selectively target specified NNR subtypes in five therapeutic focus areas: pain, smoking cessation, addiction, obesity and Parkinson's disease. In February 2010, GlaxoSmithKline announced plans to cease discovery research in selected neuroscience areas, specifically including pain. Discussions between the Company and GlaxoSmithKline regarding the effects of its strategic change on the alliance are ongoing.

Under the agreement, the Company has agreed, for specified periods of time, to use diligent efforts to conduct research activities designed to discover product candidates that target specified NNR subtypes, to develop the product candidate identified as the lead for each therapeutic focus area of the alliance through a Phase 2 proof of concept trial and to develop up to two other product candidates for each therapeutic focus area to a specified stage of preclinical development. With respect to each therapeutic focus area in the alliance, if the Company achieves clinical proof of concept with respect to a lead product candidate, GlaxoSmithKline would have an exclusive option for an exclusive license to that lead product candidate and up to two other product candidates in development in the alliance for the same therapeutic focus area on a worldwide basis. If GlaxoSmithKline exercises its option and pays the applicable exercise fee, GlaxoSmithKline would become responsible for using diligent efforts to conduct later-stage development and commercialization of the lead product candidate at its sole expense. GlaxoSmithKline's exclusive license would include all fields of use other than those indications for which the Company has granted development and commercialization rights for product candidates under its 2005 agreement with AstraZeneca focused in cognitive disorders.

The terms of the alliance provide for the Company to conduct its research and development activities under the agreement at its sole expense. The Company is, however, eligible to receive contingent milestone payments from GlaxoSmithKline as product candidates subject to the alliance advance through preclinical and clinical development.

Under the agreement and a related stock purchase agreement, GlaxoSmithKline made an initial payment to the Company of $20,000,000 and purchased 1,275,502 shares of the Company's common stock for an aggregate purchase price of $15,000,000 on July 27, 2007. The purchase price paid by GlaxoSmithKline reflected an aggregate deemed premium of $3,521,000, based on the closing price of the Company's common stock on the trading day immediately preceding the date that agreements were signed and announced. The Company deferred recognition of both the initial payment made by GlaxoSmithKline and the deemed premium paid for the shares of the Company's common stock purchased by GlaxoSmithKline and is recognizing both into revenue on a straight-line basis over the estimated nine-year period of the Company's research and early development obligations

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

13. Strategic Alliance and Collaboration Agreements—(continued)

under the agreement. The Company recognized $2,613,000 of the initial payment and deemed premium as revenue for each of the years ended December 31, 2009 and 2008 and $1,125,000 of the initial payment and deemed premium as revenue for the year ended December 31, 2007.

The Company is also eligible to receive additional payments from GlaxoSmithKline, contingent upon the achievement of specified discovery, development, regulatory and commercial milestones in each therapeutic focus area of the alliance, as well as stepped double-digit royalties dependent on any future sales for any product licensed by GlaxoSmithKline. The Company would recognize any revenue based on the achievement of milestones under the agreement upon achievement of the milestone event if the Company determines that the revenue satisfies the revenue recognition requirements for immediate recognition under its revenue recognition policy (see Note 2). The amounts that the Company may receive will depend on the success of the Company's research and development activities, the timing and achievement of the discovery, development, regulatory and commercial milestone events and whether GlaxoSmithKline exercises any options that are triggered under the agreement.

In December 2007, the Company received a $6,000,000 payment from GlaxoSmithKline upon the achievement of a specified milestone event under the agreement. The Company determined the payment did not meet each of the conditions of its revenue recognition policy (see Note 2) required for recognition of the full amount into revenue upon achievement of the milestone. Specifically, based on the progress of this product candidate as of inception of the agreement, achievement of this milestone was reasonably assured within the meaning of the Company's revenue recognition policy. Accordingly, the Company recorded the payment as deferred revenue and is recognizing it into revenue on a straight-line basis over the estimated period of the Company's research and early development obligations under the agreement. The Company recognized $692,000 of the payment as revenue for each of the years ended December 31, 2009 and 2008 and recognized $58,000 of the payment as revenue for the year ended December 31, 2007.

In addition to the $6,000,000 payment discussed above, the Company has received an aggregate of $4,000,000 in payments from GlaxoSmithKline for achievement of various milestone events under the agreement related to progress in the Company's preclinical programs, including $2,500,000 and $1,500,000 for the years ended December 31, 2009 and 2008, respectively. The Company immediately recognized the full amount of each payment as revenue upon achievement of the corresponding milestone event because each event met each of the conditions required for immediate recognition under its revenue recognition policy (see Note 2).

14. Selected Quarterly Financial Data (unaudited)

	2009 Quarter			
	First	Second	Third	Fourth
	(in thousands, except share and per share amounts)			
Net operating revenues	$ 6,141	$ 2,830	$ 12,663	$ 3,428
Operating (loss) income	(5,052)	(9,855)	1,204	(26,622)
Income tax benefit	73	—	10	5
Net (loss) income	(4,677)	(9,654)	1,334	(26,407)
Basic net (loss) income per share(1)(2)	$ (0.19)	$ (0.39)	$ 0.05	$ (0.96)
Diluted net (loss) income per share	$ (0.19)	$ (0.39)	$ 0.05	$ (0.96)
Weighted average common shares outstanding—basic(2)	24,964,909	24,966,347	25,126,823	27,465,714
Weighted average common shares outstanding—diluted(2)	24,964,909	24,966,347	26,943,535	27,465,714

TARGACEPT, INC.

NOTES TO FINANCIAL STATEMENTS—(continued)
DECEMBER 31, 2009

14. Selected Quarterly Financial Data (unaudited)—(continued)

	2008 Quarter			
	First	Second	Third	Fourth
	(in thousands, except share and per share amounts)			
Net operating revenues	$ 4,276	$ 5,156	$ 4,135	$ 6,518
Operating loss	(6,700)	(7,433)	(8,162)	(5,849)
Net loss attributable to common stockholders	(5,781)	(6,803)	(7,648)	(5,429)
Weighted average common shares outstanding—basic(2)	$ (0.24)	$ (0.27)	$ (0.31)	$ (0.22)
Weighted average common shares outstanding—basic and diluted(2)	23,834,425	24,905,965	24,945,523	24,964,373

(1) Per common share amounts for the quarters and full years have been calculated separately. Accordingly, the sum of quarterly amounts may not equal the annual amount because of differences in the weighted average common shares outstanding during each period, principally due to the effect of share issuances by the Company during the year.

(2) Diluted weighted average common shares outstanding are identical to basic weighted average common shares outstanding and Diluted EPS is identical to Basic EPS for the first, second and fourth quarters of 2009 and for all quarters of 2008 because common share equivalents are excluded from the calculations of diluted weighted average common shares outstanding for those quarters, as their effect is antidilutive.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

Not applicable.

Item 9A. Controls and Procedures.

(a) *Evaluation of Disclosure Controls and Procedures*. Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures in accordance with Rule 13a-15(b) under the Exchange Act as of the end of the period covered by this annual report. In designing and evaluating our disclosure controls and procedures, our management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives, and our management necessarily applied its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of the end of the period covered by this annual report, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is (a) accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure and (b) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

(b) *Management's Report on Internal Control Over Financial Reporting*. Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or Rule 15d-15(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, the principal executive and principal financial officers and effected by the board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may lessen. Our management, including our chief executive officer and chief financial officer, assessed the effectiveness of our internal control over financial reporting as of December 31, 2009 using the criteria established in a report entitled "Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission" and in accordance with the interpretive guidance issued by the SEC in Release No. 34-55929. Based on its assessment, our management concluded that, as of December 31, 2009, our internal control over financial reporting was effective.

Our independent registered public accounting firm has issued an audit report on the effectiveness of our internal control over financial reporting as of December 31, 2009. The report appears below.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders of
Targacept, Inc.

We have audited Targacept, Inc.'s internal control over financial reporting as of December 31, 2009, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Targacept, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Targacept, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on the COSO criteria.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of Targacept, Inc. as of December 31, 2009 and 2008, and the related statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2009 and our report dated March 11, 2010 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Raleigh, North Carolina
March 11, 2010

(c) *Changes in Internal Controls*. No change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) occurred during the quarter ended December 31, 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

Information called for by this Item may be found in our definitive Proxy Statement in connection with our 2010 Annual Meeting of Stockholders to be filed with the SEC under the captions “Board of Directors and Management,” “Corporate Governance” and “Section 16(a) Beneficial Ownership Reporting Compliance” and is incorporated by reference in this Item 10.

Code of Business Conduct and Ethics

We have adopted a code of business conduct and ethics that applies to all of our directors and officers and other employees, including our principal executive officer, principal financial officer and principal accounting officer. This code is publicly available on our website at www.targacept.com. To the extent permissible under applicable law, the rules of the SEC or NASDAQ listing standards, we intend to post on our website any amendment to the code of business conduct and ethics, or any grant of a waiver from a provision of the code of business conduct and ethics, that requires disclosure under applicable law, the rules of the SEC or NASDAQ listing standards.

Item 11. Executive Compensation.

Information called for by this Item may be found in our definitive Proxy Statement in connection with our 2010 Annual Meeting of Stockholders to be filed with the SEC under the captions “Executive Compensation” and “Corporate Governance” and is incorporated by reference in this Item 11.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Information called for by this Item may be found in our definitive Proxy Statement in connection with our 2010 Annual Meeting of Stockholders to be filed with the SEC under the captions “Security Ownership of Certain Beneficial Owners and Management” and “Equity Compensation Plan Information” and is incorporated by reference in this Item 12.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

Information called for by this Item may be found in our definitive Proxy Statement in connection with our 2010 Annual Meeting of Stockholders to be filed with the SEC under the captions “Certain Relationships and Related Person Transactions” and “Corporate Governance” and is incorporated by reference in this Item 13.

Item 14. Principal Accounting Fees and Services.

Information called for by this Item may be found in our definitive Proxy Statement in connection with our 2010 Annual Meeting of Stockholders to be filed with the SEC under the caption “Independent Registered Public Accounting Firm Fee Information and Audit Committee Pre-Approval Policy” and is incorporated by reference in this Item 14.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a)(1) *Financial Statements.* For a list of the financial statements included in this annual report, see “Index to the Financial Statements” on page 87.

(a)(2) *Financial Statement Schedules.* All schedules are omitted because they are not applicable or because the required information is shown under Item 8, “Financial Statements and Supplementary Data.”

(a)(3) *Exhibits.* The list of exhibits filed as a part of this annual report is set forth on the Exhibit Index immediately preceding such exhibits and is incorporated by reference in this Item 15(a)(3).

(b) *Exhibits*. See Exhibit Index.

(c) *Separate Financial Statements and Schedules*. None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: March 11, 2010

Targacept, Inc.

By: /S/ J. DONALD DEBETHIZY
J. Donald deBethizy
Chief Executive Officer and President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated. Each person whose signature appears below hereby constitutes and appoints J. Donald deBethizy, Alan A. Musso and Peter A. Zorn, and each of them singly (with full power to each of them to act alone), as such person's true and lawful attorneys-in-fact and agents, with full power of substitution and re-substitution, to sign any and all amendments to this Annual Report on Form 10-K and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as such person might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or any of them or any of their substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Signature	Title	Date
/S/ J. DONALD DEBETHIZY **J. Donald deBethizy**	Chief Executive Officer, President and Director (principal executive officer)	March 11, 2010
/S/ ALAN A. MUSSO **Alan A. Musso**	Vice President, Chief Financial Officer and Treasurer (principal financial officer and principal accounting officer)	March 11, 2010
/S/ MARK SKALETSKY **Mark Skaletsky**	Chairman of the Board of Directors	March 11, 2010
/S/ M. JAMES BARRETT **M. James Barrett**	Director	March 11, 2010
/S/ CHARLES A. BLIXT **Charles A. Blixt**	Director	March 11, 2010
/S/ JULIA R. BROWN **Julia R. Brown**	Director	March 11, 2010
/S/ G. STEVEN BURRILL **G. Steven Burrill**	Director	March 11, 2010
/S/ ERROL B. DE SOUZA **Errol B. De Souza**	Director	March 11, 2010
/S/ ALAN W. DUNTON **Alan W. Dunton**	Director	March 11, 2010
/S/ JOHN P. RICHARD **John P. Richard**	Director	March 11, 2010
/S/ RALPH SNYDERMAN **Ralph Snyderman**	Director	March 11, 2010

EXHIBIT INDEX

Exhibit Number	Description
3.1	Fourth Amended and Restated Certificate of Incorporation of the Company (incorporated by reference to Exhibit 4.1 to the Company's Registration Statement on Form S-8, as filed with the SEC on May 8, 2006 (Registration No. 333-133881))
3.2	Bylaws of the Company, as amended and restated January 9, 2009 and further amended effective as of August 6, 2009 (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K, as filed with the SEC on August 11, 2009)
4.1	Specimen common stock certificate (incorporated by reference to Exhibit 4.1 to Amendment No. 3 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 16, 2006 (Registration No. 333-131050))
4.2(a)	Third Amended and Restated Investor Rights Agreement, dated as of May 12, 2004, by and among the Company and certain stockholders of the Company (incorporated by reference to Exhibit 4.2(a) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
4.2(b)	Amendment No. 1, dated December 6, 2004, to Third Amended and Restated Investor Rights Agreement, dated May 12, 2004 (incorporated by reference to Exhibit 4.2(b) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
4.2(c)	Amendment No. 2, dated March 16, 2006, to Third Amended and Restated Investor Rights Agreement, dated May 12, 2004 (incorporated by reference to Exhibit 4.2(c) to Amendment No. 4 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 24, 2006 (Registration No. 333-131050))
10.1*	Form of Indemnification Agreement between the Company and each of its directors and officers (incorporated by reference to Exhibit 10.1 to Amendment No. 3 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 16, 2006 (Registration No. 333-131050))
10.2(a)	Lease Agreement, effective August 1, 2002, by and between the Company and Wake Forest University Health Sciences (incorporated by reference to Exhibit 10.2(a) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.2(b)	First Lease Amendment, effective as of January 1, 2005, to Lease Agreement effective August 1, 2002, by and between the Company and Wake Forest University Health Sciences (incorporated by reference to Exhibit 10.2(b) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.2(c)	Second Lease Amendment, executed June 30, 2006 effective as of March 31, 2006, to Lease Agreement effective August 1, 2002, by and between the Company and Wake Forest University Health Sciences (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 2006)
10.2(d)+	Third Lease Amendment, dated January 22, 2007 effective January 1, 2007, to Lease Agreement, effective August 1, 2002, by and between the Company and Wake Forest University Health Sciences (incorporated by reference to Exhibit 10.2(d) to the Company's Annual Report on Form 10-K for the Year Ended December 31, 2006)
10.2(e)	Fourth Lease Amendment, dated September 18, 2007 effective August 1, 2007, to Lease Agreement, effective August 1, 2002, by and between the Company and Wake Forest University Health Sciences

Exhibit Number	Description
10.2(f)	Fifth Lease Amendment, executed January 20, 2010 effective October 1, 2009, to Lease Agreement, effective August 1, 2002, by and between the Company and Wake Forest University Health Sciences
10.3	Loan Agreement, dated as of April 19, 2002, between the Company and the City of Winston-Salem (incorporated by reference to Exhibit 10.3 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.4	Loan Agreement, dated March 7, 2008, by and between the Company and Branch Banking and Trust Company (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed March 12, 2008)
10.5(a)*	Amended and Restated Targacept, Inc. 2000 Equity Incentive Plan (incorporated by reference to Exhibit 99 to the Company's Registration Statement on Form S-8, as filed with the SEC on May 8, 2006 (Registration No. 333-133882))
10.5(b)*	Form of Incentive Stock Option Agreement under Targacept, Inc. 2000 Equity Incentive Plan (incorporated by reference to Exhibit 10.5(b) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.5(c)*	Form of Non-employee Director Nonqualified Stock Option Agreement under Targacept, Inc. 2000 Equity Incentive Plan (incorporated by reference to Exhibit 10.5(c) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.5(d)*	Form of Restricted Stock Award Agreement under Targacept, Inc. 2000 Equity Incentive Plan (incorporated by reference to Exhibit 10.5(d) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.6(a)*	Targacept, Inc. 2006 Stock Incentive Plan, as amended and restated through November 28, 2007 and further amended effective June 10, 2009 (incorporated by reference to Exhibit 99 to the Company's Registration Statement on Form S-8, as filed with the SEC on June 30, 2009) (Registration No. 333-160331)
10.6(b)*	Form of Incentive Stock Option Agreement under Targacept, Inc. 2006 Stock Incentive Plan (incorporated by reference to Exhibit 10.6(a) to Amendment No. 3 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 16, 2006 (Registration No. 333-131050))
10.6(c)*	Form of Nonqualified Stock Option Agreement under Targacept, Inc. 2006 Stock Incentive Plan (incorporated by reference to Exhibit 10.6(b) to Amendment No. 3 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 16, 2006 (Registration No. 333-131050))
10.6(d)*	Form of Non-employee Director Nonqualified Stock Option Agreement under Targacept, Inc. 2006 Stock Incentive Plan (incorporated by reference to Exhibit 10.6(c) to Amendment No. 3 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 16, 2006 (Registration No. 333-131050))
10.6(e)*	Form of Restricted Stock Award Agreement under Targacept, Inc. 2006 Stock Incentive Plan (incorporated by reference to Exhibit 10.6(d) to Amendment No. 3 to the Company's Registration Statement on Form S-1, as filed with the SEC on March 16, 2006 (Registration No. 333-131050))
10.7(a)*	Employment Agreement, dated as of August 22, 2000, by and between the Company and J. Donald deBethizy (incorporated by reference to Exhibit 10.7 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.7(b)*	Amendment No. 1, dated March 13, 2008, to Employment Agreement, dated as of August 22, 2000, by and between the Company and J. Donald deBethizy (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)

Exhibit Number	Description
10.8(a)*	Employment Agreement, dated as of August 22, 2000, by and between the Company and Merouane Bencherif (incorporated by reference to Exhibit 10.8 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.8(b)*	Amendment No. 1, dated March 13, 2008, to Employment Agreement, dated as of August 22, 2000, by and between the Company and Merouane Bencherif (incorporated by reference to Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)
10.9(a)*	Employment Agreement, dated as of August 22, 2000, by and between the Company and William S. Caldwell (incorporated by reference to Exhibit 10.9 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.9(b)*	Amendment No. 1, dated March 13, 2008, to Employment Agreement, dated as of August 22, 2000, by and between the Company and William S. Caldwell (incorporated by reference to Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)
10.10(a)*	Employment Agreement, dated as of April 24, 2001, by and between the Company and Geoffrey C. Dunbar (incorporated by reference to Exhibit 10.10 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.10(b)*	Amendment No. 1, dated March 13, 2008, to Employment Agreement, dated as of April 24, 2001, by and between the Company and Geoffrey C. Dunbar (incorporated by reference to Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)
10.11(a)*	Employment Agreement, dated as of February 8, 2002, by and between the Company and Alan A. Musso (incorporated by reference to Exhibit 10.11 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.11(b)*	Amendment No. 1, dated March 13, 2008, to Employment Agreement, dated as of February 8, 2002, by and between the Company and Alan A. Musso (incorporated by reference to Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)
10.12(a)*	Employment Agreement, dated as of September 1, 2003, by and between the Company and Jeffrey P. Brennan (incorporated by reference to Exhibit 10.12 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.12(b)*	Amendment No. 1, dated December 3, 2007, to Employment Agreement, dated as of September 1, 2003, by and between the Company and Jeffrey P. Brennan (incorporated by reference to Exhibit 10.12(b) to the Company's Annual Report on Form 10-K for the Year Ended December 31, 2007)
10.12(c)*	Amendment No. 2, dated March 13, 2008, to Employment Agreement, dated as of September 1, 2003, by and between the Company and Jeffrey P. Brennan (incorporated by reference to Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)
10.13*	Employment Agreement, dated as of March 13, 2008, by and between the Company and Peter A. Zorn (incorporated by reference to Exhibit 10.8 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2008)
10.14(a)+	Amended and Restated License Agreement, dated as of March 9, 2004, by and between the Company and University of South Florida Research Foundation, Inc. (incorporated by reference to Exhibit 10.16 to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))

Exhibit Number	Description
10.14(b)+	Amendment No. 1, effective September 21, 2009, to Amended and Restated License Agreement dated March 9, 2004, by and between the Company and University of South Florida Research Foundation, Inc. (incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2009)
10.15(a)+	License Agreement, dated May 26, 1999, by and between the Company and University of Kentucky Research Foundation (incorporated by reference to Exhibit 10.18(a) to the Company's Registration Statement on Form S-1, as filed with the SEC on January 17, 2006 (Registration No. 333-131050))
10.15(b)+	Amendment No. 1, dated August 16, 2005, to License Agreement, dated May 26, 1999, by and between the Company and University of Kentucky Research Foundation (incorporated by reference to Exhibit 10.18(b) to Amendment No. 5 to the Company's Registration Statement on Form S-1, as filed with the SEC on April 6, 2006 (Registration No. 333-131050))
10.16(a)+	Collaborative Research and License Agreement, dated as of December 27, 2005, by and between the Company and AstraZeneca AB (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2006)
10.16(b)	Amendment No. 1 dated November 10, 2006 to Collaborative Research and License Agreement between the Company and AstraZeneca AB dated December 27, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006)
10.16(c)+	Amendment No. 2 dated July 8, 2009 to Collaborative Research and License Agreement between the Company and AstraZeneca AB dated December 27, 2005 (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2009)
10.17+	Exclusive License Agreement, dated January 22, 2007, by and between the Company and Yale University (incorporated by reference to Exhibit 10.20 to the Company's Annual Report on Form 10-K for the Year Ended December 31, 2006)
10.18+	Product Development and Commercialization Agreement, dated July 27, 2007, by and between the Company, on the one hand, and SmithKline Beecham Corporation, doing business as GlaxoSmithKline, and Glaxo Group Limited, on the other hand (incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2007)
10.19^	Amended and Restated Supply Agreement, effective December 3, 2009, by and among the Company, Interchem Corporation and Poli Industria Chimica, SPA
10.20^	Collaboration and License Agreement, dated as of December 3, 2009, by and between the Company and AstraZeneca AB
10.21*	Description of Annual Cash Incentive Program
10.22*	Description of Non-Employee Director Compensation Program
23.1	Consent of Ernst & Young LLP
24.1	Power of Attorney (included on signature page)
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Exhibit Number	Description
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

+ Confidential treatment has been granted with respect to certain portions of this Exhibit, which portions have been omitted and filed separately with the SEC as part of an application for confidential treatment.

^ Portions of this Exhibit have been omitted and filed separately with the Securities and Exchange Commission as part of an application for confidential treatment pursuant to the Exchange Act.

* Denotes management compensation plan or contract

Our SEC file number for documents filed with the SEC pursuant to the Securities Exchange Act of 1934, as amended, is 000-51173.

Exhibit 10.2e

NORTH CAROLINA)
)
FORSYTH COUNTY)

FOURTH LEASE AMENDMENT

This Fourth Lease Amendment (the "**Fourth Amendment**") is made effective as of the 1st day of August, 2007 (the "**Amendment Date**"), by and between Wake Forest University Health Sciences, a North Carolina non-profit corporation having its principal office in Winston-Salem, North Carolina (**"Landlord**"), and Targacept, Inc., a Delaware corporation having its principal office in Winston-Salem, North Carolina (**"Tenant**"). Unless otherwise defined herein, all of the capitalized terms of this Fourth Amendment shall have the same meanings ascribed to them in the Lease effective August 1, 2002, as amended by the First Lease Amendment effective January 1, 2005 (the "**First Lease Amendment**"), the Second Lease Amendment effective March 31, 2006 (the "**Second Lease Amendment**"), and the Third Lease Amendment effective January 1, 2007 (the "**Third Lease Amendment")** all of which are hereinafter collectively referred to as the "**Lease**."

WITNESSETH:

WHEREAS, Tenant desires to Lease from Landlord and Landlord desires to lease to Tenant an additional 704 square feet located on the Basement Level of the Building, and designated as "B17 Server Room" on the Basement Level Floor Plan attached as Exhibit A-2 upon the terms and for the rents as further set forth herein; and

NOW, THEREFORE, for and in consideration of the premises, of the rents reserved and to be paid by Tenant to Landlord, and of the additional mutual covenants of the parties, the parties hereby agree to amend the Lease as follows:

1. The Lease is amended by:

a. Deleting Exhibit A of the Lease, as amended, and substituting in lieu thereof the attached Exhibit A, describing the Demised Premises, and deleting Exhibit A-2 and substituting in lieu thereof the attached Exhibit A-2, which reflects modifications to the "One Technology Place, Basement Level Floor Plan" only; and

b. Deleting the table appearing in paragraph 3.1 of the Lease and substituting in lieu thereof the following table and accompanying notes:

"3.1 Tenant will pay annual rental pursuant to the following schedule ("rsf" indicates "rentable square foot"):

Initial Term

	Demised Premises		
Effective Date	**3rd & 4th Floors (40,432 rsf)**	**1,000 rsf 1st Floor**	**13,955 rsf 1st Floor (includes 1,000 rsf)**
Commencement Date 8/1/02	$ 36.00/rsf	—	—
Amendment Date 1/1/05-12/31/06	$ 36.00/rsf	$ 15.00/rsf	—
1/1/07-7/31/07	$ 36.00/rsf	—	$18.80/rsf Base ($21,862.83/month)
1/1/07-7/31/07	$ 36.00/rsf	—	$34.59/rsf Upfit Amortized (a total of $281,577.01 for the 7-month period)

Renewal Term

ONE TECH SPACE TERM	SF	RENT	COMMENTS	TOTAL ANNUAL (per month)
1st Floor:				
8/1/07-7/31/12	13,955	$ 18.80/rsf Base		$ 262,354.00 $(21,862.83/mo)
8/1/07-7/31/12	13,955	$ 34.59/rsf Upfit Amortized	Upfit costs of $2.5 million @ 9% / 7 years	$ 482,672.40
SUBTOTAL				**$ 745,026.40**
3rd and 4th Floor: 8/1/07-7/31/12	40,432	$ 33.60/rsf	Current rate is $36/sf to 7/31/07	$ 1,358,515.20 $ (113,209.60)
1st Floor: 8/1/07-7/31/12	2,969	$ 18.80/rsf		$ 55,817.20 $ (4,651.43)
SUBTOTAL				**$ 1,414.332.40**
Basement Level: 8/1/07-7/31/12	704	$ 10.00/rsf		$ 7,040.00 $ (586.67)
SUBTOTAL				**$ 7,040.00**
TOTAL:				**$ 2,166,398.80**
Second Floor*	20,669	20.00/rsf		$ 413,380.00 $ (34,448.33)

* if corresponding Option to Lease is exercised by Tenant

Second Renewal Term

The annual rent per rentable square foot for all of the space leased during the Second Renewal Term, if any, shall be equal to the then-existing market rate for similar space in the Piedmont Triad in North Carolina, as mutually determined in good faith by Landlord and Tenant. Unless Tenant does not have an interest in extending the term of the Lease for the Second Renewal Term, Landlord and Tenant shall exercise the requisite diligence to ensure that they mutually determine the annual rent per rentable square foot applicable to the Second Renewal Term, in writing, on or before July 31, 2011.

The annual rent payable during the Initial Term, the Renewal Term, and, if applicable, the Second Renewal Term (herein collectively "Rent") is payable in equal monthly installments in advance on the first day of each calendar month of each calendar year during the Initial Term, the Renewal Term, and, if applicable, the Second Renewal Term, prorated for any partial month. Any increases or decreases in the amount of square footage leased during a month will be adjusted in the subsequent monthly payment. Rent payments shall be payable to "Wake Forest University Health Sciences" and sent to Landlord in care of Controller's Office, Attention: Doug Edgeton, Medical Center Boulevard, Winston-Salem, NC 27157.

Except as amended herein, all the terms and conditions of the Lease remain in full force and effect.

IN WITNESS WHEREOF, Landlord and Tenant have caused this Fourth Amendment to be executed, pursuant to authority duly granted, effective as of August 1, 2007.

LANDLORD:	TENANT:
Wake Forest University Health Sciences	Targacept, Inc.
By: /s/ Douglas L. Edgeton	By: /s/ J. Donald deBethizy
Name: Douglas L. Edgeton	J. Donald deBethizy
Title Exec. VP & COO	President
Date: 9/18/07	Date: 9/14/07

Exhibit A

Demised Premises

The Demised Premises consist of the following:

- As of the Commencement Date, all of the third and fourth floors, consisting of 40,432 rentable square feet, including within the meaning of "Premises" or "Demised Premises" the entire fourth floor of the Building, to be utilized as Tenant's laboratory facilities, encompassing 20,216 rentable square feet, and 20,216 rentable square feet of general office space on the third floor;
- As of January 1, 2005, an additional 1,000 rentable square feet on the first floor of the Building, to be utilized as "Tenant's Storage Space";
- As of January 1, 2007, additional space located on the first floor of the Building, consisting of 13,955 rentable square feet (inclusive of the 1,000 rentable square feet described above), as depicted on the attached First Level Floor Plan attached hereto as a part of Exhibit A-2:

Rentable square footage*	Designation on Exhibit A-2 First Floor Plan	Color of Designated Space on Plan
6,555	Lab-1	blue
2,293	Office-1	purple
3,171	Office-2	olive
1,936	Office-5	yellow

; and

- As of August 1, 2007, further additional space located on the first floor of the Building, consisting of 2,969 rentable square feet, as depicted on the attached First Level Floor Plan attached hereto as a part of Exhibit A-2:

Rentable square footage	Designation on Exhibit A-2 First Floor Plan	Color of Designated Space on Plan
741	Office-3	beige
2,228	Office-4	salmon

- As of August 1, 2007, additional space located on the ground floor of the Building, consisting of 704 rentable square feet, as depicted on the attached Basement Level Floor Plan attached hereto as a part of Exhibit A-2;

; in each case together with rights of use of and subject to the rights of others in and to the Common Areas of the Building. Diagrams of the Demised Premises and Common Areas are as shown on the attached Exhibit A-2 (5 pages).

Exhibit 10.2f

NORTH CAROLINA)
)
FORSYTH COUNTY)

FIFTH LEASE AMENDMENT

This Fifth Lease Amendment (this "**Fifth Amendment**"), made effective as of the 1st day of October, 2009 (the "**Amendment Date**"), by and between Wake Forest University Health Sciences, a North Carolina non-profit corporation having its principal office in Winston-Salem, North Carolina ("**Landlord**"), and Targacept, Inc., a Delaware corporation having its principal office in Winston-Salem, North Carolina ("**Tenant**"), amends that certain Lease effective August 1, 2002, as amended by the First Lease Amendment effective January 1, 2005, the Second Lease Amendment effective March 31, 2006, the Third Lease Amendment effective January 1, 2007 and the Fourth Lease Amendment effective August 1, 2007 (the "**Lease**").

WITNESSETH:

WHEREAS, pursuant to paragraphs 6.2.1 and 6.2.2 of the Lease, Landlord agreed to provide the 2007 Upfitting Funding and to recover the amount thereof, with interest, through an increase to the rental rate payable by Tenant under the Lease over a specified period; and

WHEREAS Landlord and Tenant desire to amend the Lease to decrease the rental rate payable by Tenant thereunder to reflect a reduction in the interest rate applicable to the 2007 Upfitting Funding;

NOW, THEREFORE, for and in consideration of the premises, of the rents reserved and to be paid by Tenant to Landlord, and of the additional mutual covenants of the parties, Landlord and Tenant hereby agree as follows:

1. Unless otherwise defined herein, all of the capitalized terms of this Fifth Amendment shall have the respective meanings ascribed to them in the Lease.

2. The Lease is amended by:

   a. deleting the last two sentences of paragraph 6.2.2 of the Lease and substituting the following in lieu thereof:

      "If the Lease terminates upon expiration of the Renewal Term (not, for clarity, the Second Renewal Term), the amount payable to Landlord will be $658,085.71, provided that all installments of Rent have been timely paid. A schedule depicting the amortization of the 2007 Upfitting Funding (based upon a 7% interest rate from October 1, 2009) is attached to the Lease as Exhibit D.";

b. deleting the table under the heading “Renewal Term” in paragraph 3.1 of the Lease and substituting the following in lieu thereof, with the remainder of paragraph 3.1 remaining unchanged:

“BUILDING SPACE AND TERM	SF	RENT	COMMENTS	TOTAL ANNUAL RENT (per month) *prior to Fifth Amendment*	TOTAL ANNUAL RENT (per month) *as of effective date of Fifth Amendment*
1st Floor:					
8/1/07-9/30/09	13,955	$ 18.80/rsf Base		$ 262,354.00	$ 262,354.00
10/1/09-7/31/12				$ (21,862.83/mo)	$ (21,862.83/mo)
8/1/07-9/30/09	13,955	$ 34.59/rsf Upfit Amortized	Upfit costs of $2.5 million initially @ 9% / 84 months	$ 482,672.40 $ (40,222.70/mo)	n/a
10/1/09-7/31/12	13,955	$ 33.21/rsf Upfit Amortized	Upfit costs of $1.7 million @ 7% / 51 months	n/a	$ 463,437.00 $ (38,619.75/mo)
SUBTOTAL				**$ 745,026.40** **$ (62,085.53/mo)**	**$ 725,791.00** **$ (60,482.58/mo)**
3rd and 4th Floor:	40,432	$ 33.60/rsf	Current rate is $36/sf to 7/31/07	$ 1,358,515.20	$ 1,358,515.20
8/1/07-9/30/09				$ (113,209.60)	$ (113,209.60)
10/1/09-7/31/12					
1st Floor:	2,969	$ 18.80/rsf		$ 55,817.20	$ 55,817.20
8/1/07-9/30/09				$ (4,651.43)	$ (4,651.43)
10/1/09-7/31/12					
SUBTOTAL				**$ 1,414,332.40** **$ (117,861.03/mo)**	**$ 1,414,332.40** **$ (117,861.03/mo)**
TOTAL:				**$ 2,159,358,80** **$ (179,946.57/mo)**	**$ 2,140,123.40** **$ (178,343.61/mo)**
Second Floor*	20,669	20.00/rsf		413,380.00 $ (34,448.33)	$ 413,380.00 $ (34,448.33)

* if corresponding Option to Lease is exercised by Tenant”; and

c. inserting Attachment I to this Fifth Amendment at the end of the Lease as new Exhibit D.

3. Except as amended herein, all of the terms and conditions of the Lease remain in full force and effect.

IN WITNESS WHEREOF, Landlord and Tenant have caused this Fifth Amendment to be executed, pursuant to authority duly granted, effective as of the Amendment Date.

LANDLORD:

Wake Forest University Health Sciences

By: /s/ Douglas L. Edgeton
Douglas L. Edgeton
Executive Vice President & COO

Date: 1/20/2010

TENANT:

Targacept, Inc.

By: /s/ J. Donald deBethizy
J. Donald deBethizy
President

Date: 1/15/2010

Attachment I

MONTHLY ADJUSTMENT

Interest Rate Applicable to 2007 Upfitting Funding

	Prior to 10/1/2009 (9%)	On and after 10/1/2009 (7%)	Difference
10/1/2009	$ 40,222.70	$ 38,619.75	$ 1,602.94
11/1/2009	$ 40,222.70	$ 38,619.75	$ 1,602.94
12/1/2009	$ 40,222.70	$ 38,619.75	$ 1,602.94
1/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
2/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
3/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
4/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
5/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
6/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
7/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
8/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
9/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
10/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
11/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
12/1/2010	$ 40,222.70	$ 38,619.75	$ 1,602.94
1/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
2/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
3/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
4/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
5/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
6/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
7/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
8/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
9/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
10/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
11/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
12/1/2011	$ 40,222.70	$ 38,619.75	$ 1,602.94
1/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
2/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
3/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
4/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
5/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
6/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
7/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
8/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
9/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
10/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
11/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
12/1/2012	$ 40,222.70	$ 38,619.75	$ 1,602.94
1/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
2/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
3/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
4/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
5/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
6/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
7/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
8/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
9/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
10/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
11/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
12/1/2013	$ 40,222.70	$ 38,619.75	$ 1,602.94
GRAND TOTAL			**$ 81,750.19**

[********] Certain confidential information contained in this document, marked by brackets, has been omitted and filed separately with the Securities and Exchange Commission pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended.

AMENDED AND RESTATED SUPPLY AGREEMENT

entered into effective as of the date of the last party to sign below (hereinafter referred to as the "*Effective Date*")

by and among

TARGACEPT, INC., a Delaware corporation having a place of business at 200 East First Street, Suite 300 Winston-Salem, NC 27101-4165 (USA) (hereinafter referred to as "*Targacept*")

and

POLI INDUSTRIA CHIMICA, S.P.A., a corporation organized under the laws of Italy having a place of business at Via Volturno n° 41/49 - 58/64, 20089 Quinto de' Stampi, Rozzano, Milano (ITALY) (hereinafter referred to as "*Poli*")

and

INTERCHEM CORPORATION, a New Jersey corporation having a place of business at 120 Route 17 North, Suite 115 - Paramus NJ 07652 (USA) (hereinafter referred to as "*Interchem*")

(*Targacept*, *Poli* and *Interchem* collectively referred to as the "*Parties*" and each individually as a "*Party*").

WHEREAS,

- *Poli* has developed know-how to separate, manufacture and analyze substantially pure enantiomers of mecamylamine (the S(+) enantiomer of mecamylamine hereinafter referred to, together with its salts and any hydrates, solvates or crystal forms, as the "*API*");
- *Targacept* is interested in (i) contracting with *Poli* to have *Poli* conduct all steps and activities necessary to produce the *API* for use in the production of one or more final dosage forms containing or comprising the *API* (each such final dosage form hereinafter referred to as "*Product*"), such steps and activities to include, without limitation, manufacturing, processing, packaging, labeling, holding, storing, quality control testing, stability testing, releasing and shipping of the *API* and the documenting thereof (hereinafter referred to collectively as "*Manufacturing*" or, as the context requires, "*Manufacture*"), and to determine and perform all process development, analytical, validation, regulatory and other activities related to the *Manufacture* of the *API* that are necessary or advisable to be completed and documented in order to obtain approval from all applicable *Health Authorities* (as defined in Section 1.3) to market and sell *Product* worldwide (all of the foregoing, together with the production and supply of the *API* ordered by *Targacept* hereunder, hereinafter referred to collectively as the "*Poli Activities*"), and (ii) purchasing the *API* from *Poli* for the manufacturing and marketing of *Product*;
- *Interchem* shall act as *Poli*'s agent for the *Poli Activities*; and
- subject to the terms and conditions set forth herein, the *Parties* are interested in establishing a long-term relationship concerning the supply of the *API* for *Product* to be sold worldwide.

NOW, THEREFORE, the *Parties* have discussed and agreed upon this Amended and Restated Supply Agreement (hereinafter referred to as this "*Agreement*") on the terms and conditions as set out below.

1. POLI ACTIVITIES: PROJECT MANAGEMENT; STEERING COMMITTEE

1.1 *Poli* hereby agrees to perform the *Poli Activities* for the compensation and otherwise in accordance with the terms and conditions set forth herein.

1.2 Each of *Poli*, *Interchem* and *Targacept* shall appoint a representative having primary responsibility for interactions with the others (each a "*Project Manager*"). *Targacept*'s ******** shall be ********, *Poli*'s ******** shall be ******** and *Interchem*'s ******** shall be ********. Each of *Poli*, *Interchem* and *Targacept* may replace its *Project Manager* with another *Project Manager* with at least comparable expertise and authority upon written notice to the other *Parties*. The *Project Managers* shall meet (in person or by phone) at least quarterly. *Poli's Project Manager* shall keep *Targacept's Project Manager* regularly informed as to the status of the *Poli Activities.*

1.3 A Steering Committee, consisting of at least one (1) senior management representative from *Poli*, one (1) senior management representative from *Interchem* and two (2) senior management representatives from *Targacept*, shall meet periodically during the *Term* (as defined in Section 9.1(a), but at least annually. The ******** of the ******** shall be ********, ********, ******** and ********, each of whom shall be subject to replacement by the applicable *Party* from time to time during the *Term* by written notice to the other *Parties*. The Steering Committee shall: (i) oversee the achievement of the objectives of this *Agreement*; (ii) review the *Poli Activities* performed and planned to be performed (including, without limitation, *API* supplied and to be supplied under this *Agreement* and *Poli*'s production capacity); (iii) review requests by any *Health Authority*, or any *Party*, to make changes in or additions to the *Poli Activities*; (iv) review any adverse regulatory matters that may affect this *Agreement*, the *Poli Activities* or *API*; and (v) review and work diligently to resolve all matters not satisfactorily addressed by the *Project Managers* (it being understood with respect to this clause (v) that, if and to the extent reasonable and appropriate under the circumstances, *Targacept* will use commercially reasonable efforts to cause any third party engaged by *Targacept* to manufacture *Product* to participate in the discussion of any such matter that specifically involves such third party). *Poli* shall implement such changes as may be agreed upon by a majority of the members of the Steering Committee.

As used in this *Agreement*, "*Health Authority*" means any of the U.S. Food and Drug Administration or any successor agency having substantially the same functions (hereinafter referred to as the "*FDA*"), an analogous governmental or regulatory authority outside of the United States (including, without limitation, the European Medicines Agency or any successor agency having substantially the same functions (hereinafter referred to as the "*EMEA*")), or other national, international, supra-national, regional, state or local regulatory agency, department, bureau, commission, council or other governmental entity with authority over the distribution, importation, exportation, manufacture, use, administration, marketing or sale of pharmaceutical or medicinal products or health, safety or environmental matters.

1.4 *Poli* and *Interchem* shall inform *Targacept* promptly of any events that could reasonably be expected to affect the ability of *Poli* to timely and fully perform any *Poli Activities* or otherwise affect any established schedule or budget, including any unexpected adverse final or interim results or data from validation, stability or other studies.

1.5 Without limiting the generality of any other provision hereof, *Poli* shall: (i) determine those process development, analytical, validation, regulatory (e.g., submissions of *DMFs* or updates thereto) and other activities related to the *Manufacture* of the *API* that are necessary or advisable to be completed and documented in order to obtain approval from all applicable *Health Authorities* to market and sell *Product* worldwide; (ii) consult with *Targacept* with respect to the identification and performance of such activities in furtherance of their full completion and documentation prior to ********; and (iii) complete and document all such activities in full prior to ********.

2. REQUIREMENTS AND EXCLUSIVITY; MANUFACTURE OF API

2.1 The *Parties* expressly agree that as long as this *Agreement* is in force:

(i) subject to Section 3.2(e), *Targacept* shall purchase the *API* that *Targacept* requires exclusively from *Poli* through *Interchem* (hereinafter referred to as the "*Targacept Exclusivity Obligation*"); provided that, for clarity, the *Targacept Exclusivity Obligation* shall terminate and be of no force or effect (A) as provided in Sections 3.2(c), 5.3(b), 8.2 and 9.1(d), (B) as of the end of the *Term* and (C) if *Poli or Interchem* files a petition in bankruptcy, or enters into an agreement with its creditors, or applies for or consents to the appointment of a receiver or trustee, or makes as assignment for the benefit of creditors, or becomes subject to an involuntary proceeding under any bankruptcy or insolvency law that remains undismissed or unstayed for at least ******** days;

(ii) *Poli* shall produce (A) in accordance with the terms of this *Agreement* a sufficient quantity of the *API* to fulfill, and shall fulfill, all *Targacept* orders for *API* placed hereunder (subject to Section 3.2(d) and subject to the last paragraph of this Section 2.1) and (B) *API* for use in research, development, commercialization or other exploitation as a pharmaceutical exclusively for *Targacept* and, for clarity, not for any party other than *Targacept*; and

(iii) all *API* supplied by *Poli* to *Targacept* or its designee hereunder shall be provided from the *Inventory* (as defined in Section 3.3(a)), beginning when the *Inventory* first becomes required hereunder, and in any case on a "first-in, first-out" basis with the objective of maximizing the shelf life of all such *API* supplied to *Targacept* or its designee.

Notwithstanding clause (ii) above, with respect solely to (1) the *Semester* that begins July 1, 2010 and (2) the first *Semester* that begins after the *Product Launch Date*, if the *Order* provided by *Targacept* with respect specifically to such *Semester*, if any, is more than 150% of the *Forecast* most recently provided by *Targacept* with respect specifically to such *Semester*, if any, then Poli's obligation with respect to such *Order* shall be to (x) fulfill such *Order* to the extent of 150% of such *Forecast* within the timeframe called for by this *Agreement*, (y) use its best efforts to fulfill the remaining portion of such Order in excess 150% of such *Forecast* within the timeframe called for by this *Agreement* and (z) to the extent that, notwithstanding its best efforts, *Poli* is unable to fulfill the remaining portion of such Order in excess 150% of such *Forecast* within the timeframe called for by this *Agreement*, to fulfill such remaining portion as soon as possible. As used in this paragraph, the terms *Order*, *Forecast* and *Semester* are as defined in Section 3.1(a) and the term *Product Launch Date* is as defined in Section 9.1(a).

2.2 *Poli* shall: (i) conduct all of the *Poli Activities* at its facility located at its address set forth on the first page of this *Agreement* (hereinafter referred to as the "*Facility*"), unless *Targacept* shall have provided prior written consent otherwise; and (ii) maintain the *Facility* in a state of repair and operating condition and efficiency consistent with the requirements of *cGMP* (as defined in Section 5.1(a)(ii)) and all other *Applicable Regulation* (as defined in Section 4.2)

In addition, *Poli* shall not ******** prior to having (A) provided to *Targacept* at least ******** months (or ******** as *Poli* and *Targacept* expressly agree in writing) prior written notice (hereinafter referred to as a ******** subject to the proviso below, and (B) obtained all ******** if any, for such ******** from all applicable ******** provided that, if such ********: (1) is a ********, *Poli* shall (x) not be required to provide a ******** prior to making the applicable ******** if such ******** is made in accordance with ******** and, to the extent consistent with ********, a ******** and ******** in effect at the time of such ******** and (y) provide the ******** upon the ******** and (2) is or may be a ******** or a ********with respect to ********, *Poli* shall not make such ******** (x) ******** such ******** is necessary to comply with ******** or such ******** is ******** to comply with ******** but ******** and (y) if such ******** is ******** by clause (x) above, until *Poli* ******** (or, if applicable, any ******** or ******** of ********) that it has made or amended all ********, obtained all ******** or ******** from all ******** and ******** all aspects of the ******** and all aspects of the ******** or ******** of ********, in each case that it undertakes to make, amend, obtain or validate as a result of such change.

As used in this *Agreement*, the terms ******** have the meanings given to them in ********.

2.3 *Poli* shall not use in the conduct of the *Poli Activities* any equipment that has been used in connection with the manufacturing, processing, formulating, packaging, labeling, holding, storing and testing or release of any product made from animal-derived materials, genetically-modified organism, cytotoxic material, penicillin or penicillin-related compound, herbicide or pesticide.

2.4 *Poli* accepts responsibility for its safe performance of the *Poli Activities* and specifically acknowledges that the *Poli Activities* may be dangerous if performed improperly. *Poli* shall immediately notify *Targacept* of any unusual health or environmental occurrence relating to the *API* or the *Manufacture* thereof.

3. FORECASTS, ORDERS, INVENTORY

3.1 (a) At least ******** days prior to each calendar semester (i.e., January-June and July-December) (hereinafter referred to as a "*Semester*"), beginning with the *Semester* that begins July 1, 2010, *Targacept* shall provide *Poli* through *Interchem* with (i) an order for *Targacept*'s actual requirements of the *API* for such *Semester*, which shall be binding (hereinafter referred to as an "*Order*"), and (ii) forecasts of *Targacept*'s best estimate of its requirements for *API* for the following ******** *Semesters* ******** (the forecast for each such *Semester* hereinafter referred to as a "*Forecast*"), which shall be non-binding and shall be used for general planning purposes only. If, notwithstanding the foregoing, *Targacept* does not provide a *Forecast* for any one or more of the ******** or the ******** or the ******** or the ******** succeeding six-month period, , then *Targacept* shall be deemed to have provided a *Forecast* that it will not have any requirements for *API* for such period(s), but only if *Poli* or *Interchem* shall have notified *Targacept* in writing that such *Forecast* has not been received and *Targacept* shall not have provided a *Forecast* for such period(s) to *Poli* within ******** business days of its receipt of such notice. For clarity, neither *Poli* nor *Interchem* shall be required to provide such written notice.

(b) *Interchem* shall confirm receipt of each *Order* by written notice to *Targacept* within five (5) business days after receipt thereof. *Poli* shall be obligated to supply and deliver the quantity of the *API* specified in such *Order* in accordance with the delivery schedule set forth in such *Order*, except that, if any required date of delivery specified in any *Order* is less than ******** days from the date of such *Order*, *Poli*'s obligation with respect to such required date of delivery shall instead be to use its best efforts in good faith to supply and deliver on such specified delivery date the quantity of the *API* specified for delivery on such date in such *Order*. Any particular *Order* may be amended or cancelled only with the written consent of *Targacept* and *Poli*.

3.2 (a) In the event that *Poli*, at any time during the *Term*, shall have reason to believe that it will be unable timely to supply *Targacept* with the full quantity of the *API* subject to any *Order* (or any *Forecast* as if it were an *Order*), *Poli* shall promptly notify *Targacept* in writing; provided that, for clarity but without limiting the generality of the foregoing, Section 3.2(d) (and, if applicable, Section 3.2(e)) shall apply where such quantity exceeds *Poli*'s manufacturing capacity. For clarity, compliance by *Poli* with this Section 3.2(a) shall not relieve *Poli* of any other obligation or liability under this *Agreement*.

(b) Except where the required date of delivery specified in any *Order* is less than ******** days from the date of such *Order* and except as provided in Section 8.1, if *Poli* shall fail to supply the full quantity of the *API* that is specified in an *Order* for delivery on a specified date within ******** days after such specified delivery date, then, at *Targacept*'s sole discretion, *Poli* shall either (i) be relieved of any obligation to deliver the undelivered quantity of the *API* called for by such *Order* or (ii) deliver the undelivered quantity of the *API* called for by such *Order* within ******** days from the date *Targacept* notifies *Poli* of such election. If *Targacept* elects to have *Poli* supply the remaining quantity of the *API* called for by such *Order*, then *Poli* agrees that *Targacept* shall be entitled to a price reduction for the next amounts payable by *Targacept* hereunder in an amount equal to ********% of the full invoice amount (excluding any applicable value added tax (VAT) and other taxes, duties, charges and levies) that would have been payable with respect to such delayed supply of the *API* had such *API* been delivered on a timely basis for each week of delay (measured from the earliest date of delivery specified in such *Order* (but in no case less than ******** days from the date of such *Order*) with respect to the delayed supply of the *API* to the actual date of delivery of all of the delayed supply).

(c) In addition to, and not in limitation of, Section 3.2(b), if *Poli* shall fail to supply at least (x) ********% of the quantity of the *API* specified in an *Order(s)* for delivery on a specified delivery date that is at least ******** days from the date of such *Order* within ******** days after such specified delivery date for ******** consecutive specified delivery dates or (y) ********% of the quantity of the *API* specified in an *Order(s)* for delivery on a specified delivery date that is at least ******** days from the date of such *Order* for ******** consecutive specified delivery dates, for any reason (including, without limitation, an event of *force majeure*), then, upon written notice from *Targacept* to *Poli*, (i) *the Targacept Exclusivity Obligation* shall terminate and be of no force or effect and (ii) *Targacept* shall have the right to designate the foregoing as a ********.

(d) If *Poli* is not capable of *Manufacturing* sufficient quantities of *API* to fulfill any *Order* (or any *Forecast* as if it were an *Order*) because of limits of *Poli's* manufacturing capacity, then *Poli* shall provide written notice to such effect to *Targacept* within ******** business days of the date of the *Order* (or *Forecast*) and shall include in such notice a representation as to the maximum quantity of *API* that it is capable of supplying to *Targacept* thereafter. For purposes of this *Agreement*, the "*Poli Maximum*" shall be equal to (i) such maximum quantity that *Poli* has represented that it is capable of supplying or, if less, the maximum quantity of *API* that *Targacept*, acting in good faith and after making reasonable inquiry of and consulting with *Poli*, believes that *Poli* is capable of supplying to *Targacept* at any particular time or (ii) solely if applicable, such other maximum quantity of *API* that *Targacept*, *Poli* and *Interchem* may expressly agree to in a writing that references this Section 3.2(d).

(e) Notwithstanding the *Targacept Exclusivity Obligation*, upon written notice from *Targacept* to *Poli* and *Interchem*, *Targacept* shall be expressly permitted to purchase from any third party any quantity of *API* above the *Poli Maximum* (as such *Poli Maximum* exists at the time of such notice) and the giving of such notice by *Targacept* shall constitute a ********; provided that: (i) *Targacept* agrees that the ******** (ii) nothing in clause (i) is intended to affect or limit any of *Targacept*'s rights under this *Agreement* or to give rise to any commitment or obligation of *Targacept*, financial or otherwise, not expressly set forth in this Section 3.2(e); (iii) without limiting the generality of clause (ii), *Poli* acknowledges that ******** (iv) *Targacept*'s rights under this Section 3.2(e) shall continue unaffected whether or not, after the exercise of such rights, ******** and (v) for clarity, it is intended by this Section 3.2(e) that *Poli* shall continue as *Targacept*'s supplier for its requirements of *API* during the *Term* for quantities up to the *Poli Maximum*.

3.3 (a) Beginning with submission by *Targacept* of the first *Drug Approval Application*, *Poli* shall: (i) keep a level of inventory of the *API* (hereinafter referred to as the "*Inventory*") in an amount at all times at least equal to (A) ******** times the average of the ******** specified in *Targacept*'s most recent ******** for the ******** *Semesters* and ******** most recent ******** or (B) such ******** amount as *Targacept* may require by notice to *Poli* in writing (provided that *Poli* shall, upon request from *Targacept*, consider in good faith and not unreasonably reject any request by *Targacept* for *Poli* to maintain a larger *Inventory*); provided that *Poli* shall not be deemed in breach of this clause (i) where its failure to meet its obligation in this clause (i) results solely from the failure of *API Manufactured* by *Poli* to conform to the warranties set forth in Section 5.1(a) and only for so long as *Poli* is diligently working to provide replacement *API* pursuant to Section 5.3(a); (ii) maintain the Inventory in accordance with *cGMP* and in a location that is both separate from the *Facility* and approved by *Targacept*, such approval not to be unreasonably withheld; and (iii) provide a current written report to *Targacept* and *Interchem* specifying the amount of the *Inventory* and the respective manufacturing dates and expiration dates for the *Batches* comprising the *Inventory* with the delivery of the *API* for each *Order*.

As used in this Agreement, "*Drug Approval Application*" means an application to the applicable *Health Authority(ies)* in any country or region in the world to market and sell a *Product* in such country or region (including, without limitation, a new drug application or supplemental new drug application in the United States or the counterpart to a new drug application or supplemental new drug application for any country or region outside of the United States).

(b) In any case, the *Inventory* is dedicated for *Targacept*. Therefore, if any over-stock occurs, *Targacept* shall place an *Order* within the *Term* for the remaining *Inventory* regardless of the period that remains until expiration of such *Inventory*, such obligation of *Targacept* not to exceed amount required to be maintained pursuant to Section 3.3(a). For clarity, *Targacept* shall not be entitled under this *Agreement* to reject any *API* purchased from *Inventory* solely on the basis that such *API* does not comply with the expiration dating required by Section 5.1(a)(ii) if such *API* complied with such expiration dating at the time it first became *Inventory*.

(c) *Poli* shall have title to and responsibility for, and bear risk of loss, contamination and damage to, all *Inventory* until subject to an *Order* and received by *Targacept* or its designee; provided that, notwithstanding the foregoing, *Poli* shall have no responsibility for the expiration of any *API* that complied with all representations and warranties set forth in this Agreement at the time it first became *Inventory*.

3.4 Should Targacept have special requirements or scheduling needs, the Parties shall cooperate to the maximum extent and use their best efforts in order to accomplish such requirements or scheduling.

4. SHIPMENT, PRICING AND PAYMENT

4.1 It shall be *Targacept*'s responsibility to comply with all legal requirements in order to import the *API*, except that, if *API* is to be imported into the United States, it shall be *Interchem*'s responsibility to comply with all legal requirements in order to import the *API*. *Interchem* undertakes to obtain and keep valid at its cost all approvals, permissions and licenses required in order to enable the import the *API* into the United States.

4.2 It shall be *Poli*'s responsibility to comply with all laws and all rules, regulations, directives and guidance documents of the FDA and other competent *Health Authorities* (i) applicable to the *Manufacture* of the *API* and export of the *API* from Italy for use in clinical trials or for commercial sale in the United States and any other country or (ii) that create or relate to applicable environmental or safety standards or labor practices (hereinafter referred to collectively as "*Applicable Regulation*"). *Poli* undertakes to obtain and keep valid at its cost all approvals, permissions, permits and licenses required in order to conduct the *Poli Activities*.

For clarity, *Applicable Regulation* includes, without limitation, the U.S. Federal Food Drug and Cosmetic Act, as amended (hereinafter referred to as the "*FFDCA*"), Title 21, Parts 210 and 211 of the U.S. Code of Federal Regulations (hereinafter referred to as "*CFR*"), FDA Guidance for Industry Q7A (Good Manufacturing Practice Guidance for Active Pharmaceutical Ingredients), European Commission Directive 2003/94/EC, Volume 4 of The Rules Governing Medicinal Products in the European Union (EU), EC Guide to Good Manufacturing Practice for Pharmaceutical Products, EU Guidelines to Good Manufacturing Practice (GMP) and REACH regulations of December 18, 2006 (Regulation (EC) No. 1907/2006), in each case as may be amended from time to time. In the case of any conflict between the requirements of *Applicable Regulation* in a particular context, the *Applicable Regulation* with the most stringent requirement shall be operative.

4.3 Shipment, price and payment terms and conditions are stated in Annex B attached hereto and incorporated by reference herein. Changes, if any, shall be agreed upon in writing and executed by the *Parties*.

Without limiting the generality of any other provision hereof, *Poli* shall ship all *API* to *Targacept* or its designee in accordance with all *Applicable Regulation* (including, without limitation, 21 U.S. *CFR* 312.110) and, in addition and without limitation, industry standards for shipment of active pharmaceutical ingredients manufactured under *cGMP* (including, without limitation, under conditions that protect the *API* from contamination or temperature or humidity detrimental to the *API*).

5. WARRANTIES, QUALITY SPECIFICATIONS AND ACCEPTANCE/REJECTION

5.1 (a) *Poli* expressly represents, warrants and covenants that:

(i) at the time of delivery of each shipment of the *API* to *Targacept* or its designee, *Poli* shall have good title to, and the lawful right to sell, such *API* to *Targacept*;

(ii) the *API* supplied by *Poli* to *Targacept* or its designee: (A) shall be free and clear of all liens, encumbrances or other claims of any kind of any third party; (B) shall conform to and be in accordance with the technical specifications designated for the characteristics, quality, purity and testing procedures for the *API* (including, without limitation, for the raw materials used in the *Manufacture* of the *API*) set forth in Annex A attached hereto and incorporated by reference herein, as may be amended or supplemented from time to time in accordance with Section 5.1(b)(ii) (hereinafter referred to as the "*Specifications*"); (C) shall have been *Manufactured* in accordance with the *CMC Data* and current good manufacturing practices applicable to the manufacture of active pharmaceutical ingredients pursuant to *Applicable Regulation* (hereinafter referred to as "*cGMP*") and otherwise with all *Applicable Regulation*, all applicable *Registrations* and this *Agreement*; (D) shall not be adulterated or misbranded within the meaning of *Applicable Regulation* (including, without limitation, the *FFDCA*) and the European Commission Directive 2003/94/EC); (E) may lawfully be introduced into interstate commerce pursuant to the FFDCA; and (F) from and after August 1, 2012, have expiration dating of not less than five (5) years after the date of manufacture thereof; and

(iii) the *Manufacturing Process* (as defined in Section 5.1(c)) does not infringe or misappropriate, and will not infringe or misappropriate, the intellectual property or other proprietary rights of any third party.

(b) *Poli* expressly agrees that:

(i) *Poli* shall not make ******** to the ******** prior to having (A) provided to *Targacept* at least ******** months (or ******** as *Poli* and *Targacept* ******** (hereinafter referred to as a ********), subject to the proviso below, and (B) obtained all ******** if any, for ******** from all applicable ******** provided that, if such ********: (1) is a ********, *Poli* shall (x) ******** to provide a ******** if such ******** is made in accordance with ******** and, to the extent consistent with ********, a ******** and (y) provide the ******** upon the ******** and (2) is or may be a ******** with respect to ********, *Poli* ******** (x) unless either such ******** to comply with ******** or such ******** is ******** to comply with ******** but ******** months after it receives the ******** and (y) if such ******** by clause (x) above, until *Poli* receives ******** (or, if applicable, any ******** that it has ******** all ******** obtained all ******** from all ******** all ******** of the ******** and all aspects of the ******** or ******** of ******** in each case that it undertakes to ******** as a result of such ********.

(ii) *Poli* shall (1) not make any ******** to the ******** or to the ******** without the ******** not to be unreasonably withheld, and (2) make any *change*s to *the* ******** required by *Targacept* for the purpose of complying with ******** from time to time in effect in ********. In the event of ******** to *the* ******** shall ******** in order to evaluate whether an ******** to any of the ******** *if any, is* require*d a*nd *Poli* shall make each such ********.

(iii) *Poli* shall ******** to *Interchem* and to *Targacept* or its *designee* a ******** and shall not ******** that ******** set forth in Sec*tio*n 5.1*(a)*. With respect to any ******** the issuance of a ******** by *Poli* shall be deemed a ******** that such ******** conforms to the warranties set forth in Section 5.1(a).

(c) As used in this *Agreement*:

(i) "*Registrations*" means, with respect to any country, any and all technical, medical and scientific licenses, registrations, authorizations and approvals of a *Product* (including, without limitation, manufacturing approvals and authorizations, marketing authorizations, and pricing, third party reimbursement and labeling approvals related thereto) that are required by any *Health Authority* for the manufacture, distribution, use, importation, marketing or sale of such *Product* in such country, as may be amended or supplemented from time to time. For clarity but without limitation, the grant or approval of a *Drug Approval Application* is a *Registration*.

(ii) "*Manufacturing Process*" means, subject to Section 5.1(b)(i), (A) from the *Effective Date* until the *First Approval Date*, the processes (or steps thereof) and procedures for the *Manufacture* of the *API*, as set forth in or referenced by (including, without limitation, by reference to a *DMF*) the *Existing IND* (or, if applicable, an investigational new drug application or analogous foreign filing filed by *Targacept* or a licensee, collaborator or contractor of *Targacept* after the *Effective Date*), and (B) from and after the *First Approval Date*, the processes (or steps thereof) and procedures for the *Manufacture* of the *API* set forth in or referenced by (including, without limitation, by reference to a *DMF*) the *Drug Approval Application* granted or approved as of such *First Approval Date*.

(iii) "*First Approval Date*" means the date of grant or approval of the first *Drug Approval Application* in either the United States or any country or region in Europe.

(iv) "*Existing IND*" means U.S. investigational new drug application No. ********, as may be amended or supplemented from time to time.

(v) "*Batch*" means a specific quantity of the *API* that is intended to be of uniform character and quality and is produced during the same cycle of manufacture.

(vi) "*CMC Data* means, subject to Section 5.1(b)(ii), (A) from the *Effective Date* until the *First Approval Date*, the chemistry, manufacturing and controls data for the *API* set forth in or referenced by (including, without limitation, by reference to a *DMF*) the *Existing IND* (or, if applicable, the latest investigational new drug application or *Drug Approval Application* filed after the *Effective Date*, as may be amended or supplemented from time to time) and (B) from and after the *First Approval Date*, the chemistry, manufacturing and controls data for the *API* set forth in or referenced by (including, without limitation, by reference to a *DMF*) the *Drug Approval Application* granted or approved as of such *First Approval Date*.

(vii) "*Certificate of Analysis*" means a document signed by an authorized representative of the *Poli* business unit that conducted the testing described hereinafter and an authorized representative of *Poli*'s quality unit that describes the *Specifications* for, shelf life of, testing methods applied to and results of such testing of a particular *Batch* and meets *Targacept*'s purchasing specifications.

5.2 (a) *Targacept* expressly agrees that:

(i) within ******** days of delivery, it shall or shall cause its designee to (i) analyze the *API* and (ii) in the event that *Targacept* or its designee determines that such *API* does not conform to its *Specifications* (or does not comply with any other warranty set forth in Section 5.1(a)), notify in writing *Poli* and *Interchem* of its rejection (hereinafter referred to as a "*Non-Compliance*") and the basis therefor;

(ii) if *Targacept* does not notify *Poli* and *Interchem* within the ******** period specified above, the *API* shall be considered finally accepted by *Targacept*; provided that *Targacept*'s acceptance or rejection of, or failure to reject, any *Batch* shall not prejudice any rights or remedies that may be available to *Targacept* hereunder, at law or in equity arising due to a breach by *Poli* of its warranties set forth in Section 5.1(a) or any other provision of this *Agreement* with respect to such *Batch* or otherwise; and

(iii) *Targacept* will not incorporate any *Batch* that has not been analyzed by *Targacept* or its designee as provided in Section 5.2(a)(i) in the manufacture of *Product*.

(b) In the event that the basis for a *Non-Compliance* is a failure to conform with *Specifications*, *Poli* shall promptly undertake appropriate testing of a sample retained from the rejected *Batch* and notify *Targacept* whether it has confirmed the *Non-Compliance*. Should *Poli* conduct such testing and *Poli* and *Targacept* be unable thereafter to agree that a *Non-Compliance* has occurred within ******** days of the notice from *Targacept* pursuant to Section 5.2(a)(i), the matter will be referred to an independent external laboratory mutually acceptable to *Targacept* and *Poli* for testing. The conclusions of such laboratory as to whether or not a *Non-Compliance* shall have occurred, shall be final and binding and the cost of such laboratory (including, if applicable, reasonable, customary and documented out-of-pocket analytical transfer costs), shall be charged to the *Party* against which the laboratory concludes (*Targacept* or *Poli*). *Poli* and *Targacept* shall provide such laboratory with samples/counter-samples of the *API*, certificates of analysis, stability studies/data and any further documentation as may be in its possession or control and relevant to the laboratory's assessment, and the laboratory shall be directed to render its conclusions as soon as possible and in any event within ******** days after its receipt of the foregoing.

5.3 (a) If any *API* delivered to *Targacept* or its designee pursuant to this *Agreement* does not conform to the warranties set forth in Section 5.1(a) (for any reason, including, without limitation, an event of *force majeure*), then *Poli* shall reimburse within ******** business days or, if not actually paid by *Targacept*, credit *Targacept* with all costs that *Targacept* incurs with respect to such non-conforming *API* (including, without limitation, all amounts paid to *Poli* with respect to such *API* pursuant to Section 4.3, if any, any and all transportation and holding charges incurred by *Targacept* in connection with such *API* and the cost of destruction of such *API*). In addition, at *Targacept*'s sole discretion, *Poli* shall either (i) be relieved of any obligation to deliver *API* in replacement of such non-conforming API or (ii) replace the non-conforming *API* with replacement *API* that conforms to the warranties set forth in Section 5.1(a) and deliver such replacement *API* by an agreed upon date not to exceed ******** days after the date for delivery specified in the applicable *Order*. If and to the extent a reprocess procedure is included in the *U.S. DMF* (as defined in Section 11.1(a)) or otherwise in a *Registration*, *Poli* may reprocess the non-conforming *API* to bring it into compliance. If *Targacept* elects to have *Poli* replace the rejected *API*, *Poli* agrees that *Targacept* shall be entitled to a price reduction for the next amounts payable by *Targacept* hereunder in an amount equal to ********% of the full invoice amount (excluding any applicable value added tax (VAT) and other taxes, duties, charges and levies) that would have been payable with respect to such non-conforming *API* had such *API* been conforming for each week of delay in delivering conforming API (measured from the earliest date of delivery specified in the applicable *Order* with respect to the non-conforming *API* to the actual date of delivery of all replacement conforming *API*).

(b) In addition to, and not in limitation of, Section 5.3(a), if the quantity of the *API* supplied by *Poli* on a specified delivery date that conforms to the warranties in Section 5.1(a) is ******** then, upon written notice from *Targacept* to *Poli* and *Interchem*, (i) ********.

It is understood and agreed that, in the event of ************ or ************ of *API* (rather than ************) Sections 3.2(b) and 3.2(c) and not Sections 5.3(a) and 5.3(b) shall apply.

5.4 Each *Party* represents and warrants that (i) it is in existence and in good standing under the laws of its state (or country) of incorporation on the *Effective Date*, (ii) it has full corporate power to enter into and perform all of its obligations under this *Agreement* and (iii) its execution, delivery and performance of this *Agreement* have been duly authorized by all necessary corporate action. In addition, *Poli* represents and warrants that (A) there is no claim, suit, proceeding, or investigation pending or, to its knowledge, threatened against *Poli* or any affiliate thereof that might prevent or interfere with its performance of this *Agreement* and (B) as of the *Effective Date*, it has submitted the *U.S. DMF* (as defined in Section 11.1(a)) to the *FDA* and such *U.S. DMF* is correct and complete.

6. INDEMNITIES, INSURANCE AND WAIVER

6.1. Each of the *Parties* (each hereinafter referred to as an "*Indemnifying Party*") shall indemnify, defend and hold the other *Parties*, their respective affiliates and all of their respective directors, officers, employees, agents and representatives (hereinafter referred to collectively as "*Targacept Indemnitees*," "*Poli Indemnitees*" or "*Interchem Indemnitees*," as the case may be, and all together, as the "*Indemnitees*") harmless from and against any and all claims, suits, actions, demands, investigations and proceedings brought or instituted against any one or more *Indemnitees* by any third party (each such claim, suit, action, demand, investigation or proceeding hereinafter referred to as a "*Claim*"), and any and all damages, out-of-pocket losses, liabilities, costs and expenses, including reasonable attorneys' fees (collectively, "*Losses*"), arising out or resulting from (i) the breach by such *Indemnifying Party* of any of its obligations, representations or warranties under this *Agreement*, (ii) the willful misconduct, errors or omissions of such *Indemnifying Party* in the performance of this *Agreement*, or (iii) where *Poli* is the *Indemnifying Party*, any defect in the *API Manufactured* hereunder or its infringement of any process or technical data of a patent or other proprietary rights of any third party, except in each case (clauses (i), (ii) and (iii)) to the extent such *Losses* are caused by the gross negligence or willful misconduct of, or breach of this *Agreement* by, *Targacept* (where *Poli* or *Interchem* is the *Indemnifying Party*) or either *Poli* or *Interchem* (where *Targacept* is the *Indemnifying Party*).

6.2 Any *Indemnitee* seeking to enforce Section 6.1, shall:

(i) promptly (but in any event within ************ days) following receipt of written notice of the applicable *Claim*, notify the *Indemnifying Party* in writing of such *Claim*, specifying in a degree of detail reasonable under the circumstances the nature of such *Claim* and the amount of liability estimated to arise therefrom; provided that: (A) the failure to provide timely notice shall not affect the rights of the *Indemnitee* if (1) such notice is provided and (2) the failure for such notice to be timely does not materially prejudice the ability of the *Indemnifying Party* to defend or settle such *Claim*; and (B) it is understood and agreed that notice provided by *Targacept* shall be deemed provided by all *Targacept Indemnitee*s, notice provided by *Poli* shall be deemed provided by all *Poli Indemnitee*s and notice provided by *Interchem* shall be deemed provided by all *Interchem Indemnitee*s;

(ii) provide to the *Indemnifying Party* as promptly as practicable all information and documentation reasonably requested by the *Indemnifying Party* to verify the claim asserted hereunder and shall otherwise cooperate fully with the *Indemnifying Party* in all respects in the investigation and defense of such *Claim*; and

(iii) permit the *Indemnifying Party* to assume the defense of the *Claim* (and the prosecution of all *Claims* available against third parties and the right to compromise or settle, subject to Section 6.3), including the employment of counsel or accountants of the *Indemnifying Party*'s choice and at its cost and expense; provided that the *Indemnitee* shall (A) use commercially reasonable efforts (but specifically excluding settlement) to protect against further liability with respect to the *Claim* and (B) have the right to employ counsel separate from counsel employed by the *Indemnifying Party* and to participate therein, but the fees and expenses of such counsel shall be at the *Indemnitee*'s own expense.

6.3 *Targacept* shall not settle or compromise any *Claim* in a manner that imposes any restrictions or obligations on, or admits fault of, *Poli* or *Interchem* without the prior written consent of *Poli* or *Interchem*, as the case may be, and neither *Poli* nor *Interchem* shall settle or compromise any *Claim* in a manner that (i) imposes any restrictions or obligations on, or admits fault of, *Targacept* or (ii) impairs or would reasonably be expected to impair *Targacept*'s ability or right to manufacture, market or sell *API* or any *Product* or *Poli*'s ability, right or obligation to perform its obligations hereunder, in each case without *Targacept*'s prior written consent. No *Indemnifying Party* shall have any obligations hereunder with respect to any *Claim* compromised or settled without its prior written consent.

6.4 NOTWITHSTANDING ANYTHING IN THIS *AGREEMENT* TO THE CONTRARY (BUT WITHOUT AFFECTING THE *PARTIES*' RIGHTS AND OBLIGATIONS UNDER SECTION 6.1), IN NO EVENT SHALL ANY *PARTY* BE LIABLE TO ANY OTHER PARTY FOR ANY SPECIAL, INCIDENTAL, CONSEQUENTIAL, PUNITIVE OR INDIRECT DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES BASED ON LOST REVENUES OR LOST PROFITS, ARISING IN ANY WAY OUT OF THIS *AGREEMENT*, HOWEVER CAUSED AND WHETHER UNDER ANY CONTRACT, WARRANTY, TORT, NEGLIGENCE, STRICT LIABILITY OR OTHER LEGAL OR EQUITABLE THEORY, EVEN IF SUCH *PARTY* HAS BEEN ADVISED OF THE POSSIBILITY OF SUCH DAMAGES.

6.5 Each of the *Parties* will obtain and keep in full force during the *Term* and for ******** years thereafter insurance policies from reputable insurance companies recognized in both the United States and Europe. Such insurance shall provide such *Party* with insurance cover for its performance of this *Agreement* (including, without limitation, its indemnification and related obligations and, in the case of *Poli*, risk of loss, contamination and damage to the *Inventory*) of the types and not less than the levels of insurance coverage customarily maintained by companies in the pharmaceutical industry engaged in comparable activities. Each *Party* will provide the other *Party* with evidence of such insurance upon request. *Poli* shall also provide *Targacept* with copies of all insurance policies, endorsements, cover notes and other relevant documentation and information in respect of insurance maintained by *Poli* in accordance with this Section 6.5 upon request. *Poli*'s policies of insurance shall (i) be primary to any liability insurance carried by *Targacept*, which insurance shall be excess and non-contributory for such claims and (ii) be specifically endorsed to list *Targacept* as an additional insured. *Poli* shall also maintain workers' compensation insurance as required by all applicable laws, rules and regulations. At such times as *Targacept* may reasonably request in writing, *Poli* shall provide *Targacept* with certificates of insurance evidencing the insurance coverage required under this Section 6.5, which certificates shall specifically provide for at least thirty (30) days prior notice of cancellation or termination thereof. In no event shall the amounts for which a *Party* would otherwise be liable be limited to the amounts recoverable through insurance maintained by such *Party*.

7. CONFIDENTIALITY AND PUBLICITY

7.1 "*Confidential Information*" means all confidential or proprietary information that is or has been (i) disclosed by *Poli* or *Interchem* to *Targacept* or by *Targacept* to *Poli* or *Interchem* related to the *API*, *Product* or the *Manufacture*, development, marketing or sale of *API* or *Product*, including but not limited to any data, specifications, formula, methods, technologies, strategies, forecasts, plans, suppliers and business of the disclosing *Party*, and (ii) marked or otherwise identified in writing or other tangible form at the time of disclosure as "Confidential" or, if disclosed orally, reduced to a writing or other tangible form that is marked "Confidential" and delivered to the *Recipient* within ******** days after such first disclosure. Each disclosing *Party* (i) shall retain all of its right, title and interest in and to its *Confidential Information* and all patents, patent applications, copyrights and other intellectual property rights arising, created or obtained in connection therewith and (ii) represents that it has the right to disclose all *Confidential Information* that it discloses hereunder without any obligation to any third party.

7.2 Except as provided in Section 7.3, the *Party* receiving the *Confidential Information* from a disclosing *Party* (hereinafter referred to as "*Recipient*") shall use commercially reasonable efforts to maintain in confidence such *Confidential Information* and shall not disclose it to any third party without prior written approval by the disclosing *Party*.

7.3 *Recipient*'s obligations of confidentiality and non-use under Section 7.2 shall not apply to:

(i) information which at the time of disclosure is publicly available or after disclosure becomes publicly available, except as a result of any act or omission by *Recipient*;

(ii) information which *Recipient* can establish by competent proof that was lawfully in its possession at the time of disclosure by the disclosing *Party* (or thereafter is lawfully received) and was not acquired, directly or indirectly, under a confidentiality obligation; or

(iii) the disclosure of information to the extent required to be disclosed pursuant to subpoena or order by any competent court, or requested by any governmental or regulatory agency or authority (including, without limitation, any *Health Authority*), asserting jurisdiction over *Recipient*; provided that *Recipient* shall give the disclosing *Party* prompt written notice and, to the extent practicable under the circumstances, a reasonable opportunity to object to or pursue confidential treatment for such disclosure.

In addition, and notwithstanding anything herein to the contrary: (A) *Targacept* shall be expressly permitted to disclose the terms of this *Agreement* in, and to file this *Agreement* as an exhibit to, any filing with the U.S. Securities and Exchange Commission that *Targacept* determines in its sole discretion requires such disclosure or exhibit; (B) each *Recipient* may disclose a disclosing *Party*'s *Confidential Information* solely: (1) on a need-to-know basis to such *Recipient*'s legal and financial advisors; (2) as reasonably necessary in connection with an actual or potential (x) license (or sublicense) of intellectual property rights of such *Recipient* or permitted assignment of this *Agreement*, (y) debt or equity financing of such *Recipient* or (z) *Change of Control* involving such *Recipient*; provided that, with respect to any such disclosure pursuant to this clause (2), the third-party recipient of such *Confidential Information* of the disclosing *Party* is subject to a written agreement that requires such third-party recipient to maintain the confidentiality of such *Confidential Information* with terms at least substantially as restrictive as Sections 7.2 and 7.3; or (3) as reasonably necessary to file, prosecute or maintain *Patent Rights* or to file, pursue or defend litigation related to *Patent Rights*; and (C) *Targacept* may disclose a disclosing *Party*'s *Confidential Information* that relates to the *API* or the *Manufacture* or characterization thereof or that is relevant to submissions to the *FDA* or other *Health Authority* to a third party recipient or proposed recipient of a *Technology Transfer* (as defined in Section 10.2(a)).

As used in this *Agreement*:

(aa) "*Change of Control*" means, with respect to any *Party*, (1) a merger, consolidation, acquisition, share exchange or other similar transaction involving such *Party* and any third party which results in the holders of the outstanding voting securities of such *Party* immediately prior to such merger, consolidation, share exchange or other similar transaction ceasing to hold more than fifty percent (50%) of the combined voting power of the surviving, purchasing or continuing entity immediately after such merger, consolidation, share exchange or other similar transaction, (2) any transaction or series of related transactions in which any "person," as such term is used in Sections 13(d) and 14(d) of the Securities Exchange Act of 1934, as amended (hereinafter referred to as the "*1934 Act*"), together with any of such person's "affiliates" or "associates," as such terms are used in the *1934 Act*, becomes the beneficial owner of fifty percent (50%) or more of the combined voting power of the outstanding securities of such *Party* or (3) the bona fide sale or other transfer to a third party (other than a third party who or that controls, is controlled by or is under common control with such *Party*, where "control" means the power to direct or cause the direction of the management or policies, whether through the ownership of voting securities, by contract or otherwise) of all or substantially all of such *Party*'s assets that relate to this *Agreement*; and

(bb) "*Patent Rights*" means (1) issued and unexpired letters patent in any country, including extensions, registrations, confirmations, reissues, supplementary protection certificates and re-examinations thereof, (2) patent applications pending in any country, including all provisional applications, substitutions, continuations, continuations-in-part, divisionals and renewals thereof, and (3) foreign counterparts of any of the foregoing.

7.4 *Recipient* shall not use the *Confidential Information* for any purpose other than the performance of its obligations and exercise of its rights under this *Agreement*, without first entering into a specific agreement with the disclosing *Party*.

7.5 *Recipient* shall restrict access to the *Confidential Information* received from a disclosing *Party* to the minimum number of employees necessary for the purposes of performance of its obligations or exercise of its rights under this *Agreement* and shall ensure that the persons in question are obligated to *Recipient* by terms at least substantially as restrictive as those contained in this *Agreement* to keep such *Confidential Information* confidential.

7.6 *Recipient*'s obligation to confidentiality and non-use under this *Agreement* shall survive expiration or early termination of this *Agreement* for ************ years thereafter.

7.7 The *Parties* agree that monetary damages may or may not be a sufficient remedy for unauthorized disclosure of *Confidential Information* and that the disclosing *Party* may or may not be entitled, without waiving any other rights or remedies, to such injunctive or equitable relief as may be deemed proper by a court having jurisdiction.

7.8 *Targacept* shall not use the name of *Poli* or *Interchem*, and neither *Poli* nor *Interchem* shall use the name of *Targacept*, without such *Party*'s prior written consent; provided that this Section 7.8 shall not restrict a *Party* from identifying another *Party* or *Parties* or its or their performance of this *Agreement* to any *Health Authority* or as required by applicable law, rule or regulation (including, without limitation, the rules of any securities exchange or quotation system on which a *Party*'s securities are listed or traded).

8. FORCE MAJEURE

8.1 (a) Except as otherwise expressly set forth in this *Agreement*, any delay in the performance of any of the duties or obligations hereof (except the payment of money) of any *Party* shall not be considered a breach of this *Agreement* and shall not give rise to any claim for damages, provided that such delay has been caused by or is the result of an act of God or other unforeseeable, extraordinary cause beyond the control and without the fault or negligence of the *Party* so affected (including but not limited to, acts of war (whether or not war be declared), insurrections, riots, embargoes, shortages of materials, labor disputes such as strikes, lockouts or boycotts, fires, explosions, floods, earthquakes or mudslides). The *Party* so affected shall give prompt notice in writing of such event of *force majeure* to the other *Parties* and provide all the particulars thereof and shall take and keep the other *Parties* informed about whatever reasonable steps are necessary to relieve the effect of such event of *force majeure* as rapidly as possible, when the affected *Party* reasonably expects to resume performance in whole or in part of its obligations hereunder and when the event of *force majeure* has ceased to exist. Failure to give such notice to the other *Parties* shall cause the *Party* claiming an event of *force majeure* not to be relieved from performing its obligations under this *Agreement*.

(b) A *Party* affected by an event of *force majeure* shall use its best efforts to remedy, remove or mitigate such event and the effects thereof as soon as practicable; provided that, for clarity and without limitation, this Section 8.1(b) shall not require that the affected *Party* settle a strike or other labor controversy.

8.2 If any event of ******** interrupts or otherwise negatively affects *Poli*'s ability to produce *API* for at least ******** days, then, unless *Poli* establishes to the reasonable satisfaction of *Targacept*, acting in good faith, that *Poli* will remain capable of meeting *Targacept's* requirements for *API* at all times thereafter without interruption, upon written notice from *Targacept* to *Poli*, (i) ******** and (ii) ********.

9. TERM AND TERMINATION; NON-RENEWAL FEE; NON-EXCLUSIVITY FEE

9.1 (a) This *Agreement* shall commence on the *Effective Date* and shall (i) remain in force until the fifth (5th) anniversary of the *Product Launch Date* (hereinafter referred to as the "*Initial Term*"), and (ii) thereafter be subject to automatic renewal in two (2) year increments as provided in Section 9.1(b) (each such two-year period hereinafter referred to as a "*Renewal Term*" and all such *Renewal Terms*, if any, together with the *Initial Term*, hereinafter referred to as the "*Term*"), in each case (clauses (i) and (ii)) unless earlier terminated in accordance with Section 9.2.

As used in this *Agreement*, "*Product Launch Date*" means the date of the first occurrence of a sale, transfer or disposition for value by *Targacept* (or a licensee, collaborator or contractor of *Targacept*) of any *Product* for use or consumption in any country or region in the world following the grant or approval of a *Drug Approval Application* for such *Product* in such country or region. *Targacept* shall use commercially reasonable efforts to notify *Poli* and *Interchem* of the *Product Launch Date*.

(b) Unless *Poli* or *Targacept* gives the other written notice of non-renewal of this *Agreement* (hereinafter referred to as a "*Non-Renewal Notice*") by the date that is ******** months prior to the expiration of (i) the *Initial Term*, the *Term* shall be deemed to be automatically extended for one (1) *Renewal Term* or (ii) if applicable, the then-current *Renewal Term*, the *Term* shall be deemed to be automatically extended for the next *Renewal Term*.

(c) In the event that *Targacept* gives *Poli* (but not, for clarity, if *Poli* gives *Targacept)* a *Non-Renewal Notice* by the date that is ******** months prior to the expiration of the *Initial Term* or the then-current *Renewal Term*, as the case may be, *Targacept* will pay a "*Non-Renewal Fee*" to *Poli* in an amount determined and to be paid as follows. In the event *Targacept* gives *Poli* a *Non-Renewal Notice*, *Poli* shall provide a copy of such *Non-Renewal Notice* to *Interchem*.

(i) The amount of the *Non-Renewal Fee* shall be determined by ******** from the ******** shown in column D in the table below the sum of (1) ******** pursuant to Section 10.3 and (2) ******** pursuant to Section 9.1(d).

A	B	C	D
	Average quantity (kg/*Commercial Supply Year* ********) of *API* subject to non-canceled Orders provided during:		
Non-renewal upon expiration of:	*Applicable Commercial Supply Years*	*Quantity (kg)*	******** (EURO €)
the ********	the last ******** *Commercial Supply Years* of the *Initial Term* (i.e., months ******** through ******** and ******** through ******** that follow the ********	not more than ********	********
		between ******** and ********	********
		higher than ********	********
the ********, if any	the ******** *Commercial Supply Years* in the ******** *Term*	not more than ********	********
		between ******** and ********	********
		higher than ********	********
the ********, if any	the ******** *Commercial Supply Years* in the ******** *Term*	not more than ********	********
		between ******** and ********	********
		higher than ********	********
a ********, if any	the ******** *Commercial Supply Years* in such ******** *Term*	not more than ********	
		between ******** and ********	********
		higher than ********	

(1) As used in this *Agreement*, ******** means a consecutive ******** month period that begins on the *Product Launch Date* or an anniversary thereof.

(2) The ******** fee shall be ********% of the unadjusted fee that would have been payable if non-renewal had instead occurred at the end of the immediately preceding ******** *Term*. As illustrative examples, if non-renewal occurs at the end of the (a) ******** *Term*, if any, the ******** fee would be €******** (applicable average quantity not more than ********kg), €******** (applicable average quantity between ********kg and ********kg) or €******** (applicable average quantity higher than ********kg), (b) *********Term*, if any, the ******** fee would be €******** (applicable average quantity not more than ********kg), €******** (applicable average quantity between ********kg and ********kg) or €******** (applicable average quantity higher than ********kg) or (c) ******** *Term*, if any, the ******** fee would be €******** (applicable average quantity not more than ********kg), €******** (applicable average quantity between ********kg and ********kg) or €******** (applicable average quantity higher than ********kg).

(ii) The *Non-Renewal Fee* shall be due and payable ******** days after the later of the date (A) of receipt by *Targacept* of a proper invoice from *Poli* therefor and (B) on which *Targacept* confirms in writing that a ******** has occurred. Notwithstanding the preceding sentence, if the production of more than ******** *Batches* that conform to the ******** and the ********and test within acceptable ranges on relevant parameters as the *Batches* validated by *Poli* for commercial use is required to achieve a ********, then (1) ********% of the ******** *Fee* shall be due and payable ******** days after the later of the date (x) of receipt by *Targacept* of a proper invoice from *Poli* therefor and (y) on which *Targacept* confirms in writing the production of ******** *Batches* that meet the foregoing conditions and (2) ********% of the ******** *Fee* shall be due and payable ******** days after the later of the date (x) of receipt by *Targacept* of a proper invoice from *Poli* therefor and (y) on which *Targacept* confirms in writing that a ******** has occurred.

(iii) For purposes of this Agreement, a ******** shall have occurred if and at such time as *Targacept* confirms in writing that *Targacept* or its designee has produced ******** *Batches* (or such ******** number of *Batches* as may then be required by ******** or by any ******** to conclude that the performance of the ******** by *Targacept* or such designee is validated) that conform to the ******** and the ********and test within acceptable ranges on relevant parameters as the *Batches* validated by *Poli* for commercial use.

(d) *Targacept* shall have the right to continue this *Agreement* on a non-exclusive basis after the *Initial Term* or any *Renewal Term* by giving written notice to *Poli* (hereinafter referred to as a ******** *Notice*") (i) by the date that is ******** months prior to the expiration of the ******** *Term* or the then-current ******** *Term*, as the case may be, and (ii) that includes a commitment to purchase for the ******** *Term* or the ******** *Term*, as the case may be, from *Poli* through *Interchem* at least a ******** percentage (from ********% to ********%) of the *API* that *Targacept* requires for such ******** *Term* (hereinafter referred to as the ********).

In the event *Targacept* provides a ******** *Notice*, (A) the *Targacept* ******** *Obligation* shall ******** and (B) a ******** (hereinafter referred to as a ******** *Fee*") will be due from *Targacept* to *Poli* in an amount equal to:

(1) if the ******** is above ********%, ********% of the amount of the ******** *Fee* that would have become payable by *Targacept* pursuant to Section 9.1(c)(i) if such ******** *Notice* had been a ******** or

(2) otherwise (but subject to Section 9.1(e)), a ******** of the amount of the ******** *Fee* that would have become payable by *Targacept* pursuant to Section 9.1(c)(i) if such ******** *Notice* had been a ********equal to ********% minus the ******** (as an illustrative example, if the ********were ********%, the ******** *Fee* would be ********% of the amount that would have become payable by *Targacept* pursuant to Section 9.1(c)(i) if such ******** had been a ********;

such ******** to be payable by *Targacept* within ******** days after the later of the date (x) of receipt by *Targacept* of a proper invoice from *Poli* therefor and (y) on which *Targacept* confirms in writing that a ******** has occurred. Notwithstanding anything in this *Agreement* to the contrary, in no event shall more than one ******** *Fee* be payable by *Targacept*.

(e) If the ********is not above ********%, *Poli* shall have the right, by written notice to *Targacept* given within fifteen (15) days after the date of the ******** to reject such ******** and thereby deem such ******** to be a ********, in which event Section 9.1(c) (including, without limitation, the ******** *Fee* determined as provided in Section 9.1(c)(i)) shall thereupon apply in lieu of Section 9.1(d).

9.2 (a) This *Agreement* may be terminated upon the mutual written agreement of *Targacept* and *Poli*.

(b) Either *Targacept* or *Poli* shall be entitled to terminate this *Agreement* by giving written notice to the other if (i) *Targacept*, in the case of termination by *Poli*, or *Poli* or *Interchem*, in the case of termination by *Targacept*, commits any material breach of this *Agreement* and, if such breach is capable of being cured, fails to cure the breach within ********days after receipt of written notice of such breach from the non-breaching *Party* or (ii) *Targacept*, in the case of *Poli*, or *Poli* or *Interchem*, in the case of *Targacept*, files a petition in bankruptcy, or enters into an agreement with its creditors, or applies for or consents to the appointment of a receiver or trustee, or makes as assignment for the benefit of creditors, or becomes subject to an involuntary proceeding under any bankruptcy or insolvency law that remains undismissed or unstayed for at least ******** days.

(c) *Targacept* shall have the right, at its sole discretion, to terminate this *Agreement* at any time immediately upon written notice to *Poli* and *Interchem*:

(i) if the *First Approval Date* has not occurred on or before the seventh (7^{th}) anniversary of the *Effective Date*;

(ii) upon the circumstances described in Section 3.2(c) or Section 5.3(b);

(iii) upon the failure of *Poli* or *Interchem* to obtain or maintain any licenses, registrations or approvals required by this *Agreement* or *Applicable Regulation* in connection with the *Manufacturing* of the *API* or performance of any other *Poli Activities*, either generally or specifically at the *Facility*;

(iv) upon a *Change of Control* of *Poli* or *Interchem* (subject to Section 10.3(b)), if *Targacept* shall reasonably in good faith (A) determine that it has a conflict of interest with the surviving, purchasing or continuing entity in such *Change of Control* or (B) believe that such surviving, purchasing or continuing entity may not meet *Poli's* obligations hereunder.

(v) upon the attempted assignment or delegation by *Poli* or *Interchem* of any of its rights or performance hereunder not in accordance with Section 14(a);

(vi) if, with respect to any *Patent Rights* owned or licensed by *Targacept* that claim or cover the composition of matter, pharmaceutical composition or a method of use of the S(+) enantiomer of mecamylamine hydrochloride, *Poli* or *Interchem* files an action for a declaratory judgment of invalidity of such *Patent Rights*, initiates a re-examination proceeding with respect to such *Patent Rights*, or otherwise challenges the scope, validity or enforceability of such *Patent Rights*; or

(vii) if at any time during the *Term* the *Inventory* is not maintained at the level required by Section 3.3(a)(i); provided that, solely with respect to this clause (vii), *Targacept* shall not have the right to terminate this *Agreement* until it has made reasonable inquiry of (or used commercially reasonable efforts to make reasonable inquiry of) *Poli* as to the cause for the failure to maintain the required *Inventory*.

9.3 (a) The effective date of any termination pursuant to Section 9.2 shall be the last day of the *Term*.

(b) Expiration or termination of this *Agreement* by any means and for any reason shall not relieve the *Parties* of any obligation accruing concurrently therewith or prior thereto and shall be without prejudice to the rights and remedies of any *Party* with respect to any breach of any of the provisions of this *Agreement* occurring prior to such expiration or termination.

(c) In particular but without limiting the generality of Section 9.3(b), upon expiration or termination of this *Agreement* for any reason:

(i) outstanding unpaid true and correct invoices issued by *Interchem* on behalf of *Poli* in respect of the *API* delivered prior to the effective date of such expiration or termination shall be paid by *Targacept* as provided in Annex B;

(ii) unless agreed in writing otherwise by *Targacept* and *Poli*, *Poli* shall be required to produce and deliver compliant *API*, and *Targacept* shall be required to purchase (subject to its right of rejection under this Agreement), the *API* subject to *Order*s placed prior to such expiration or termination of this *Agreement*; and

(iii) *Targacept* shall purchase from *Poli* through *Interchem* the remaining *Inventory*, provided that *Targacept*'s obligation shall (A) not exceed the amount of *Inventory* required to be maintained pursuant to Section 3.3(a) and (B) be subject to its right of rejection under this Agreement.

9.4 The provisions of Sections 3.3(c), 4.1, 4.2, 5.1, 5.3(a), 9.3, 9.4, Articles 6, 7, 8, 10, 11, 12 and 14 (excluding clauses (g) and (i) thereof) and paragraphs 3 (last sentence only) and 4 of Annex B (including, for purposes of interpreting any such section, article or annex, the portions of all other sections or articles that are themselves referenced in such section, article or annex or define terms that are used in such section, article or annex), shall survive and continue following the last day of the *Term*. In addition all obligations and warranties of *Poli* or *Interchem* hereunder as applied to the *Poli Activities* completed as of the last day of the *Term* shall survive and continue following the last day of the *Term*.

10. TECHNOLOGY TRANSFER; IP LICENSE

10.1 As used in this *Agreement*:

(a) ******** means the ******** to occur of:

(i) if no other clause of this Section 10.1(a) applies, *Targacept* gives written notice to *Poli* on or after the ******** of the ******** directing *Poli* to transfer the ******** to *Targacept* or any designee of *Targacept* (hereinafter referred to as an ********);

(ii) any ******** designated by *Targacept* as a ******** pursuant to any provision of this *Agreement*;

(iii) either *Targacept* or *Poli* gives a ******** to the other;

(iv) *Targacept* gives a ******** to *Poli*; or

(v) the ******** day of the *Term*.

(b) "*Poli IP*" means: (i) U.S. Patent No. ******** all counterparts of U.S. Patent No. ******** outside of the United States and all other *Patent Rights* owned by *Poli* that claim priority to the patent application from which U.S. Patent No. ******** issued, if any; (ii) all ideas, concepts, discoveries, inventions, developments, improvements, know-how, expertise, trade secrets, designs, devices, equipment, process conditions, specifications, algorithms, notation systems, works of authorship, computer programs, technologies, formulas, techniques, methods, procedures, synthesis information, assay systems, applications, experimental results, data (including, without limitation, analytical, toxicological, pharmacological, clinical, bioequivalence and stability data), documentation, records, reports, enzymes, reagents, proteins, peptides, organisms, formulations and samples owned or controlled by *Poli*, in each case that relates generally or specifically to the *Manufacturing* of the *API*; and (iii) all *Patent Rights* that claim or cover any of the subject matter of clause (ii).

10.2 (a) Upon a ********, *Poli* shall (i) provide *Targacept* and any third party designated by *Targacept* with all reasonable assistance required by *Targacept* or such designee to transfer the ******** to *Targacept* or such designee (hereinafter referred to as the ********) and (ii) use its best efforts to achieve a ******** within ******** months (or, if a ******** constitutes the ******** months) after the ********.

(b) In particular but without limiting the generality of Section 10.2(a), *Poli* shall:

(i) make available to *Targacept* or its designee all ******** and ******** relating to the ******** (including, without limitation, all of the ********) and all documentation constituting material support, performance advice, shop practice, specifications as to materials to be used and control methods that are necessary or useful to enable *Targacept* or its designee to use and practice the ********) and quantities of intermediates and active ingredients reasonably requested by *Targacept* or its designee to validate ******** by or on behalf of *Targacept* or its designee using the ********;

(ii) cause all ********and ******** of *Poli* to meet with employees or representatives of *Targacept* or its designee at both the ******** and the ******** of *Targacept* or its designee, at mutually convenient times, to assist with the working up and use of the ******** and with the training of *Targacept*'s or its designee's personnel to the extent necessary or useful to enable *Targacept* or its designee to use and practice the ********;

(iii) without limiting the generality of clause (ii), cause all ******** and ******** and ******** of *Poli* to meet with employees or representatives of *Targacept* or its designee at both the ******** and the ******** of *Targacept* or its designee and make available all ******** at mutually convenient times, to support and execute the transfer of all applicable ******** and the ******** thereof (including, without limitation, all applicable ******** and ********and ********;

(iv) take such steps as are necessary or useful to assist in reasonable respects *Targacept* or its designee in obtaining any necessary ********or ******** from the ******** and all other applicable ******** with respect to *Targacept* or its designee's ********; and

(v) provide such other assistance as *Targacept* or any *Targacept* designee may reasonably request to enable *Targacept* or its designee to ******** and ******** the ********and otherwise to ********.

In addition, without intending to limit or modify the ******** of the *Targacept* ******** *Obligation* and without requiring the disclosure of any information that is not otherwise required by this *Agreement*, *Poli* hereby grants to *Targacept*, a ******** (subject to the terms of this *Agreement* and, for clarity, all ******** owned or licensed by *Targacept*), ******** (except as provided in clause (ii) of the proviso below), ******** to all ******** to make, have made, develop, have developed, use, sell, have sold, offer for sale and import ******** (or intermediates thereof) and any ******** and otherwise to exploit such ******** in all respects in connection therewith (hereinafter referred to as the ********); provided that the ******** shall ******** and be of no force or effect upon effectiveness of ******** of this *Agreement* by (A) *Poli* pursuant solely to Section 9.2(b)(i) for an uncured material breach of this *Agreement* by *Targacept* or (B) *Targacept* pursuant solely to Section 9.2(c)(i).

10.3 (a) If a ******** constitutes the ******** *Targacept* shall pay to *Poli* (i) ******** Euros (€********) within ******** days after receipt of an invoice from *Poli* that includes a certification that *Poli* has initiated the ******** and (ii) ******** Euros (€********) within ******** days after the ******** of the date (A) of receipt by *Targacept* of a proper invoice from *Poli* therefor and (B) on which *Targacept* confirms in writing that a ******** has occurred.

(b) If the ******** day of the *Term* both (i) arises from the termination of this *Agreement* by *Targacept* pursuant solely to Section 9.2(c)(iv) and (ii) constitutes the ******** then Section 9.1(c) shall apply as if *Targacept* gave a ******** as of the last day of the *Term*, except that the ********shall be ********% of the amount determined in accordance with Section 9.1(c)(i).

(c) With respect to all ******** (other than a ********that is described in any of Sections 3.2(c), 3.2(e), 5.3(b), 8.2, 10.1(a)(iii), 10.1(a)(iv), 10.3(a) or 10.3(b)), *Targacept* will reimburse *Poli* for its actual and reasonable out-of-pocket expenses to perform the ******** within ******** days after the later of the date (A) of receipt by *Targacept* of a proper invoice from *Poli* therefor and (B) on which *Targacept* confirms in writing that a ******** has occurred.

11. DMFs AND OTHER REGULATORY MATTERS; RECALLS; INTELLECTUAL PROPERTY MATTERS

11.1 (a) *Poli* shall: (i) to the extent permitted by *Applicable Regulation*, keep and maintain on file with the *FDA* a drug master file for the *API* using the procedure of 21 CFR 314.420 (hereinafter referred to as the "*U.S. DMF*") and keep and maintain on file with each other *Health Authority* as may be directed by *Targacept* from time to time a drug master file (or analogous foreign submission) for the *API* using the appropriate procedure permitted by *Applicable Regulation* (each hereinafter referred to as an "*Ex-U.S. DMF*" and, together with the *U.S. DMF*, the "*DMFs*"); (ii) with respect to each of the *DMFs*, allow *Targacept* to reference the relevant information and documentation therein (including, without limitation, by executing promptly following *Targacept*'s request a letter of access or comparable document reasonably required to provide such right of reference); (iii) maintain and keep current and complete any and all such *DMFs* at all times during the *Term*; and (iv) not interfere in any way with the right of reference noted above.

(b) Upon the request of *Targacept* made not more frequently than once per calendar year, *Poli* shall make all *DMFs* available for audit at the *Facility* in their entirety to an independent third party selected by *Targacept* and reasonably acceptable to *Poli* for purposes of confirming the adequacy and completeness of, and *Poli*'s compliance with, each *DMF*, subject to such independent third party's execution of a confidentiality agreement in a form reasonably acceptable to *Poli*; provided that it is understood and expressly agreed that such third party shall be permitted to provide to *Targacept* its conclusions as to the adequacy and completeness of each *DMF* and, if applicable, to identify any inadequacies or omissions and provide to *Targacept* its recommendations to address the same.

(c) Notwithstanding Section 11.1(a), with respect to any particular information or documentation relevant to specific methods of *Manufacture* or characterization of the *API* (including, without limitation, the *Manufacturing Process*) or any other information specific to the *API* and relevant to submissions to the *FDA* or other *Health Authority*, *Poli* may provide such information or documentation to *Targacept* or its designee (and, in such event, as between *Poli* and *Interchem*, *Poli* shall provide such information or documentation to *Targacept* or its designee through *Interchem*) in lieu of including such information or documentation in the applicable *DMF*. In such event, *Poli* shall provide such information or documentation in a manner to enable its timely submission for review and approval by the *FDA* or other *Health Authority*, as applicable.

11.2 In addition to, and without limiting the generality of, Section 11.1, *Poli* agrees to provide to *Targacept* or its designee such information and assistance relating to the *Manufacture* or characterization of the *API* as *Targacept* may reasonably require for purposes of applying for and maintaining any or all *Registrations* for *Product* worldwide. It is understood and agreed that *Targacept* does not warrant or guarantee that it will require any *API* or any particular quantity of *API* in any particular period, that it will seek to obtain or that it will obtain approval to conduct clinical trials of *Product* or that it will seek to obtain or obtain approval for commercial sale of *Product* in any country.

11.3 If *Poli* receives notice of (i) any serious adverse drug experience (as defined under 21 CFR 312.32) or any analogous term under *Applicable Regulation* pertaining to *API* or *Product* or (ii) any complaint or event that may necessitate a field alert under 21 CFR 314.81(b)(1) or any other *Applicable Regulation*, relating to *Product*, *Poli* shall notify *Targacept* within twenty-four (24) hours after its receipt of such notice. *Poli* shall investigate all reports of a quality complaint with respect to the *API* or *Product*, and each *Party* shall cooperate in such investigations in all reasonable respects.

11.4 In the event that *Targacept* shall be required, or shall decide, to recall or withdraw, or effect a field alert with respect to, any *Product* containing or comprising *API* supplied by *Poli* pursuant to this *Agreement*, then *Poli* and *Interchem* shall assist *Targacept* in all reasonable respects in implementing such recall, withdrawal or field correction. If such recall, withdrawal or field correction is initiated because of (i) any failure of such *API* to conform to the warranties set forth in Section 5.1(a) or otherwise because of the negligence or willful misconduct of *Poli*, *Poli* shall promptly reimburse *Targacept* for all costs associated with such recall, withdrawal or field correction (together with all amounts paid by *Targacept* hereunder with respect to the *API* contained in or comprising the *Product* subject to such recall, withdrawal or field correction) or (ii) a latent defect in such *API* (i.e., a defect, other than the failure of such *API* to conform to the *Specifications*, that is not discovered by *Targacept* or its designee in the conduct of reasonable analysis in accordance with Section 5.2(a)(i)), but where such *API* has, until its expiration date, been stored in accordance in all material respects with *Applicable Regulation*) that affects its quality or functionality and to which clause (i) does not apply, *Poli* shall promptly reimburse *Targacept* for 50% of all costs associated with such recall or withdrawal (together with 50% of all amounts paid by *Targacept* hereunder with respect to the *API* contained in or comprising the recalled or withdrawn *Product*).

11.5 All rights and licenses now or hereafter granted to *Targacept* under or pursuant to this *Agreement* (including, without limitation, Section 10.2), are rights to "intellectual property" (as defined in Section 101(35A) of Title 11 of the United States Code, as amended, such Title 11 hereinafter referred to as the "*Bankruptcy Code*"). In connection with the practice of the *License* (as defined in Section 10.2), *Poli* hereby grants to *Targacept*: (i) the right of access to (A) laboratory notes, notebooks and records related to the *API* required to be maintained by *Poli* under this *Agreement* or *Applicable Regulation* and (B) regulatory filings and approvals (including, without limitation, the *DMFs*); and (ii) the right of access to and the right to obtain possession of and to benefit from (A) copies of data generated in or arising out of research of the *API*, (B) laboratory samples, (C) samples of the *API*, (D) formulas, including the *Specifications*, and (E) all other embodiments of such intellectual property, all of which constitute "embodiments" of intellectual property pursuant to Section 365(n) of the Bankruptcy Code, whether any of the foregoing are in *Poli*'s possession or control or in the possession and control of third parties. *Poli* shall not interfere with *Targacept*'s exercise of rights and licenses to intellectual property licensed hereunder and embodiments thereof in accordance with this *Agreement* and agrees to use its best efforts to assist *Targacept* to obtain such intellectual property and embodiments thereof in the possession or control of third parties as reasonably necessary or desirable for *Targacept* to exercise such rights and licenses in accordance with this *Agreement*. The *Parties* acknowledge and agree that (x) none of the payments payable by *Targacept* under this *Agreement* constitute "royalties" within the meaning of Bankruptcy Code §365(n) or relate to licenses of intellectual property hereunder and (y) *Targacept* shall have the right to sublicense to third parties all rights granted or licensed to *Targacept* under this *Agreement* (including, without limitation, the rights of access granted in this Section 11.5). To effectuate the purposes of this Section 11.5 outside of the United States, all provisions of applicable law analogous to the *Bankruptcy Code* shall be deemed to apply and to be incorporated *mutatis mutandis* into this Section 11.5.

12. GOVERNING LAW, ARBITRATION

12.1 This *Agreement* shall be construed and interpreted in accordance with the laws of the State of New York (USA), without regard to the principles of conflicts of laws. The *Parties* agree to exclude the application of the United Nations Convention on Contracts for the International Sale of Goods to this *Agreement*.

12.2 Except as expressly provided in Section 12.3(c), no *Party* shall institute a proceeding in any court or administrative agency to resolve any dispute, claim or other controversy arising out of or relating to this *Agreement*, or any alleged breach thereof, before that *Party* has sought to resolve the dispute through the processes set forth in Section 12.3.

12.3 (a) The *Parties* shall use commercially reasonable efforts to resolve amicably any dispute, claim or other controversy arising out of or relating to this *Agreement*, or any alleged breach thereof, through mutual discussions and negotiations among a senior executive of each *Party*.

(b) If such senior executives do not resolve the dispute, claim or other controversy within ******** days after any *Party* requests a discussion among senior executives pursuant to this Section 12.3, such dispute, claim or other controversy shall be settled by means of arbitration before neutral arbitrator(s) administered by the International Chamber of Commerce in accordance with its commercial arbitration rules in effect on the date of the request for arbitration (hereinafter referred to as the "*Rules*").

The seat of arbitration shall be London, England and the language shall be English, which the arbitrators shall speak fluently. Written proofs in English shall be admitted to the arbitration proceedings without need of their translation. The number of arbitrators appointed pursuant to the *Rules* shall be one (1) arbitrator agreed by the *Parties*. If the *Parties* are unable to agree, then each *Party* shall appoint one (1) arbitrator, of its own choice and the arbitrators so appointed shall further appoint a third arbitrator. No arbitrator may be appointed who has previously been instructed, consulted, employed or engaged by any *Party* or its attorneys and solicitors within the preceding ************ years, unless the nature of such relationship is fully disclosed and consented to by the *Parties*.

The arbitrator(s) shall have no power to add to, subtract from or modify any of the terms or conditions of this *Agreement*, shall base any award on applicable laws and judicial precedent and include in such award a statement of the reasons upon which the award is based. The award to be rendered shall be final and conclusive and binding upon all the *Parties* without any right to appeal or other review and may be entered in and enforced by any court having jurisdiction, except that any award rendered against *Targacept* shall only be enforceable by the federal or state courts located in Forsyth County, North Carolina. The costs of the arbitration proceedings shall be charged to the losing *Party*; provided that, if *Poli* or *Interchem* is the losing *Party*, the costs shall be a joint and several obligation of each of *Poli* and *Interchem*.

All applicable statutes of limitation and defenses based upon the passage of time shall be tolled while the procedures specified in this Section 12.3(b) are pending, and each *Party* shall take such action, if any, required to effectuate such tolling. Each *Party* shall be required to continue to perform its obligations under this *Agreement* pending final resolution of any dispute, claim or other controversy arising out of or relating to this *Agreement* or any alleged breach thereof.

(c) Notwithstanding Section 12.3(b) or any other provision hereof, any *Party* shall be entitled to seek interim or provisional judicial relief, in the form of a temporary restraining order, preliminary injunction or other interim equitable relief to protect the interests of such *Party* prior to or during an arbitration proceeding pursuant to Section 12.3(b), which relief may be made permanent by the arbitrator(s).

13. QUALITY AGREEMENT

Each of the *Parties* agree to work diligently and in good faith to prepare, negotiate and execute a complementary agreement covering quality matters with respect to the *Manufacture* of the *API* hereunder within ******** months following the *Effective Date*. Upon execution, such complementary quality agreement shall be deemed a part hereof and incorporated by reference herein. To the extent of any conflict between this *Agreement* and terms of such complementary quality agreement, the complementary quality agreement shall control solely with respect to matters that are both solely operational and designed to ensure compliance with *cGMP* and this *Agreement* shall control with respect to all other matters.

14. MISCELLANEOUS

(a) This *Agreement* or any rights or performance hereunder may be assigned or delegated (including for clarity, but without limitation, subcontracted) only (i) with the written authorization of *Poli*, in the case of *Targacept*, or *Targacept*, in the case of *Poli* or *Interchem*, in each case, not to be unreasonably withheld, conditioned or delayed, (ii) by *Targacept* to a licensee of intellectual property rights relating to the *API* or to mecamylamine or (iii) to the bona fide successor to all or substantially all of the business of a *Party* (whether by merger, consolidation, asset transfer or similar transaction) to which this *Agreement* relates. Any other assignment or delegation (including, without limitation, subcontract) is void.

(b) This *Agreement*, including for clarity the attached Annexes (which are an integral part of it) and the complementary quality agreement contemplated by Article 13, (i) amends and restates in its entirety the Supply Agreement dated July 23, 2001 among *Poli*, *Interchem* and *Targacept*, as assignee of Layton Bioscience Inc., as amended (hereinafter referred to as the "*2001 Agreement*"), except solely that the *Parties'* respective representations, warranties and obligations set forth in one or more of Sections 6, 11 and 13 of the *2001 Agreement* as applied to "Product" (as defined thereunder) manufactured or delivered thereunder to *Targacept* or its designee, and activities performed with respect thereto, by *Poli* prior to the *Effective Date* shall continue in full force and effect and (ii) constitutes the entire agreement between the *Parties* and supersedes all previous negotiations and arrangements between the *Parties* relating to the subject matter of this *Agreement*. For clarity, (A) all "Isomers" (as defined in the *2001 Agreement*) manufactured or delivered thereunder to *Targacept* or its designee, and activities performed with respect thereto, by *Poli* prior to the *Effective Date* (including, without limitation, in connection with the written orders placed thereunder effective May 26, 2007 and April 28, 2009) shall be deemed to be *API* manufactured or delivered, or activities performed with respect thereto, under this *Agreement* and (B) the Services Agreement dated July 28, 2006 among *Poli*, *Interchem* and *Targacept*, as amended, shall continue in full force and effect. Each *Party* confirms that it is not relying on any representation, warranty or communication of any other *Party*, except for those specifically set forth in this *Agreement*.

(c) This *Agreement* may be executed in up to three counterparts (which may be exchanged by facsimile or PDF with the same legal effect as if original signatures were exchanged), each of which shall be deemed an original and all of which together shall constitute one and the same agreement.

(d) No modifications of this *Agreement* shall be binding unless agreed upon in writing and executed by authorized representatives of *Targacept* and *Poli*. Failure by any *Party* to enforce any rights under this *Agreement* shall not be construed as a waiver of such rights nor shall a waiver by such *Party* in one or more instances by construed as constituting a continuing waiver or as a waiver in other instances.

(e) In the event of any provision of this *Agreement* being declared invalid, void, illegal or otherwise unenforceable by any judicial or other competent authority, the validity, legality and enforceability of the rest of the provisions of this *Agreement* shall not be in any way affected or impaired. The *Parties* shall endeavour to amend such invalid, void, illegal or otherwise unenforceable provision in a reasonable manner to achieve the intention of the *Parties* reflected herein.

(f) Except to the extent otherwise expressly provided in this *Agreement*, any remedy set forth in any section of this *Agreement* (including, without limitation, Sections 3.2(b), 3.2(c), 5.3(a), 5.3(b), 6.1 and 11.4) shall be in addition to, and not in limitation of, any other rights or remedies that may be available hereunder, at law or in equity.

(g) Each *Party* agrees to execute, acknowledge and deliver such additional documents and instruments and to do all such other acts as may be necessary or appropriate in order to carry out the purposes and intent of this *Agreement*.

(h) The headings used in this *Agreement* are intended for convenience only and shall not be considered part of the written understanding between the *Parties*. The *Parties* acknowledge and agree that: (i) each *Party* and its counsel reviewed and negotiated the terms and provisions of this Agreement and have contributed to its drafting; (ii) the rule of construction to the effect that any ambiguities are resolved against the drafting *Party* shall not be employed in the interpretation of this *Agreement*; and (iii) the terms and provisions of this Agreement shall be construed fairly as to each *Party* and not in a favor of or against either *Party*, regardless of which *Party* was generally or primarily responsible for the drafting of this *Agreement*.

(i) Except as provided in this paragraph, any notice required under this *Agreement* shall be effective only if it is in writing and (i) delivered in person, (ii) deposited with a internationally recognized overnight courier service, or in the mails, postage prepaid and return receipt requested, in either case addressed to the applicable address set forth on the first page of this *Agreement*, or (iii) otherwise transmitted and confirmed received by an authorized officer of the recipient to which such notice is provided. Notices shall be effective upon actual receipt or, if earlier, notices (A) deposited with an overnight courier service shall be effective one (1) business day after deposit (if sent within the United States) and upon actual receipt (if sent from or to outside of the United States) and (B) sent by mail shall be effective ******** business days after deposit, postage prepaid, in the mails (if sent within the United States) and upon actual receipt (if sent from or to outside of the United States). Each *Party* may designate by written notice to the other *Parties* in accordance herewith any other address to which notices shall be sent.

(j) Each of the *Indemnitees* shall be a third party beneficiary of Sections 6.1 and 6.2, entitled to enforce the terms thereof at law or in equity. Except as expressly provided in this paragraph, this *Agreement* is not intended to, and does not, confer any rights or remedies upon any individual, entity or governmental body or agency who or that is not a *Party* and no individual, entity or governmental body or agency who or that is not a *Party* shall have any right to enforce this *Agreement* at law or in equity.

(k) It is expressly agreed that *Poli* and *Interchem*, on the one hand, and *Targacept*, on the other hand, shall be independent contractors and that the relationship between them shall not constitute a partnership, joint venture or agency. Neither *Poli* or *Interchem*, on the one hand, nor *Targacept*, on the other hand, shall have the authority to bind the other without the prior consent of the other. All individuals employed by a *Party* shall be employees of such *Party* and not of any other *Party* and all costs and obligations incurred by reason of any such employment shall be for the account and expense of such employer *Party*.

(l) Each of *Poli* and *Interchem* acknowledges the validity of the title of *Targacept* in and to any and all trademarks that may be used in conjunction with any *Product* (or *API*). No right, title or interest in and to such trademarks is granted by this *Agreement*.

IN WITNESS WHEREOF, authorized representatives of the *Parties* have signed this *Agreement* on the respective dates set forth below.

For and on behalf of :
TARGACEPT INC.

Date: December 3, 2009

Mr. J. Donald deBethizy
(President and CEO)

/s/ J. Donald deBethizy

Date:

Mr.
( )

For and on behalf of :
POLI INDUSTRIA CHIMICA S.P.A.

Date: December 2, 2009

Mr. Alberto Mangia
(Managing Director)

/s/ Alberto Mangia

Date: December 2, 2009

Mr. Guido Puricelli
(Legal Affairs)

/s/ Guido Puricelli

For and on behalf of :
INTERCHEM CORPORATION

Date: December 2, 2009

Mr. Ronald J. Mannino
(Chairman)

/s/ Ronald J. Mannino

Date: December 2, 2009

Mr. Joseph M. Pizza
(President)

/s/ Joseph Pizza

ANNEX A

SPECIFICATIONS

Appearance:********

Identification: ********

Acidity: ********
Loss on drying: ********
Water (KF): ********
Residue on ignition: ********
Specific optical rotation: ********
Heavy metals: ********
Chlorides content: ********
Assay (GC): ********

Related substances (GC): ********
Enantiomeric excess: ********

Residual solvents (GC): ********

Microbial contamination: ********

ANNEX B

SHIPMENT, PRICING AND PAYMENT

The ******** price for the *API* ******** and performance of all other *Poli Activities* shall be as provided in the table and accompanying notes below. Invoice currency shall be in Euros. For clarity, ******** means that, except for import taxes and duties to be paid by *Targacept* consistent with the DDU Incoterm, no other amounts shall be invoiced to, or payable by, *Targacept*.

	Quantity (kg)/Calendar Year*	Pricing (Euro€/kg)
Initial Term	first ********	********
	next ********	********
	next ********	********
	next ********	********
	above ********	********
After the *Initial Term*	See paragraph 1 below.	

* Refers to the quantity of *API* included in *Orders* provided during a calendar year (January 1 through December 31).

An example, for illustrative purposes, is set forth below.

Calendar Year	Order Date	Quantity	Price Invoiced/kg	x	Number of kg =	€
********	********	********kg	€********/kg	x	********kg =	€********
			€********/kg	x	********kg =	€********
	********	********kg	€********/kg	x	********kg =	€********
					Calendar Year Total:	€********
********	********	********kg	€********/kg	x	******** kg =	€********
			€********/kg	x	********kg =	€********
			€********/kg	x	********kg =	€********
	********	********kg	€********/kg	x	******** kg =	€********
			€********/kg	x	********kg =	€********
			€********/kg	x	********kg =	€********
					Calendar Year Total:	€********

1. (A) If the *Term* continues after the ******** *Term*, subject to subparagraph (B) below, the pricing for the *API* to be applicable during the ******** *Term* or the ******** *Term*, as the case may be, shall be subject to review and adjustment pursuant to a written request by either *Targacept* or *Poli*, at intervals of not less than ******** months, to take into account any actual increase or decrease in *Poli*'s ********. All adjustments to the price based on an increase or decrease in cost for a particular calendar year shall be given effect on January 1 of the next calendar year. All calculations made pursuant to this paragraph shall be made in accordance with *Poli*'s standard accounting practices and with generally accepted accounting principles in the United States and shall be consistently calculated on the same basis and utilizing the same criteria as is utilized for other active pharmaceutical ingredients manufactured by *Poli*.

(B) In no event shall any increase in the pricing for *API* made pursuant to this paragraph 1 (stated as a percentage of the then-current pricing) for any year ******** (i) the ********of the ******** for each of the ******** calendar years in the ******** (for ********as reported by the Bureau of Labor Statistics of the U.S. Department of Labor (final compilation published at the end of each calendar year) or (ii) ********%.

2. Upon each shipment of the *API*, *Interchem* (on behalf of *Poli*) shall promptly invoice *Targacept* therefor in a form reasonably acceptable to *Targacept* and in accordance with this *Annex B*. Payment shall be due ******** days after receipt by *Targacept* of such invoice; provided that if *Targacept* shall reject such shipment pursuant to Section 5.2, then payment shall be due, if at all, within ******** business days after receipt by *Targacept* of notice from the ******** that the invoiced *API* is in fact conforming or, subject to application of any applicable credit, the receipt by *Targacept* of replacement *API*, as the case may be.

3. *Targacept* shall make all payments pursuant to this Annex B by check payable to Interchem Corporation and sent to 120 Route 17 North, Suite 115 - Paramus NJ 07652 (USA), Attn: Diana Tate or wire transfer to a bank account designated in writing by *Interchem*. Each of *Poli* and *Interchem* acknowledges and agrees that it is the ********** obligation of *Interchem* to disburse payment to *Poli* for the *Poli Activities* performed hereunder and that, except as otherwise expressly provided in Sections 9.1(c), 9.1(d), 10.3(a) and 10.3(c) (in each case, if and to the extent applicable), *Targacept* shall have no payment or other financial obligation to *Poli* whatsoever.

4. *Interchem* shall keep accurate records of all shipments of the *API* and invoice calculations hereunder and, upon the request of *Targacept*, shall permit *Targacept* or its designee to examine such records during normal business hours for the purpose of verifying the correctness of all such calculations.

Exhibit 10.20

[********] Certain confidential information contained in this document, marked by brackets, has been omitted and filed separately with the Securities and Exchange Commission pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended.

Execution Copy

COLLABORATION AND LICENSE AGREEMENT

BETWEEN

ASTRAZENECA AB

AND

TARGACEPT, INC.

TABLE OF CONTENTS

Schedules

COLLABORATION AND LICENSE AGREEMENT

This **COLLABORATION AND LICENSE AGREEMENT** (this "**Agreement**") is entered into as of the third day of December 2009 (the "**Execution Date**") by and between Targacept, Inc., a Delaware corporation having its principal place of business at 200 East First Street, Winston-Salem, North Carolina 27101 ("**Targacept**"), and AstraZeneca AB, a company limited by shares organized and existing under the laws of Sweden having a principal place of business at V-Malarehamnen 9, S-151 85 Södertälje, Sweden ("**AstraZeneca**"). Targacept and AstraZeneca are each referred to herein by name or as a "**Party**" or, collectively, as the "**Parties**."

RECITALS

WHEREAS, Targacept has completed a Phase 2 human clinical trial of its product candidate known as Amplixa™ as an augmentation (add-on) treatment for major depressive disorder;

WHEREAS, AstraZeneca possesses expertise in the research, development, manufacturing and commercialization of pharmaceuticals for human use and is interested in developing and commercializing Amplixa, and potentially other Compounds (as defined below), as a drug product(s); and

WHEREAS, the Parties desire to establish a worldwide, strategic collaboration for the continued development of Amplixa, and potentially for the development of other Compounds, and, if successful, Marketing Approval and Commercialization for Licensed Products (as defined below), subject to the terms and conditions set forth herein.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Parties hereby agree as follows:

ARTICLE 1
DEFINITIONS

As used in this Agreement, the following terms shall have the respective meanings set forth or referenced below.

1.1 "**AAA**" means the American Arbitration Association.

1.2 “**Acceptance**” means, with respect to an NDA or sNDA, (a) the date on which the FDA notifies AstraZeneca that it has accepted such NDA or sNDA for filing or (b) if, after the Effective Date, Applicable Laws in the U.S. Territory do not require such an affirmative notice from the FDA for an NDA or sNDA to be deemed accepted for filing, the date on which such NDA or sNDA is deemed accepted for filing under Applicable Laws in the U.S. Territory.

1.3 “**Acquisition Transaction**” has the meaning set forth in Section 6.1.3(b)(ii).

1.4 “**Acting Party**” has the meaning set forth in Section 7.12.4.

1.5 “**Additional Development Activities**” means, with respect to an Additional Development Project, all Development activities related to obtaining and maintaining Regulatory/Pricing Approval in the Territory with respect to the form, formulation, method of delivery or Indication that is the subject of such Additional Development Project.

1.6 “**Additional Development Costs**” means, with respect to an Additional Development Project, all Development Costs attributable to the Additional Development Activities with respect to such Additional Development Project.

1.7 “**Additional Development Costs ********”** has the meaning set forth in Section **********.

1.8 “**Additional Development Project**” means any discrete collection of Development (and, for clarity, not Commercialization) activities that are not Initial Development Activities.

1.9 “**Additional Notice Deadline**” has the meaning set forth in Section 3.9.1(c)(iv).

1.10 “**Adjunct Therapy**” means, with respect to a Licensed Product, that such Licensed Product is any of (a) labeled for use, (b) the subject of a Drug Approval Application for approval to be labeled for use or (c) the subject of a Phase 3 Clinical Trial for evaluation, in each case (clauses (a), (b) and (c)) as an augmentation (add-on) or adjunctive treatment (or other term reflecting the concurrent use of two (2) or more pharmaceutical products) with one or more other pharmaceutical products to treat, prevent, cure or delay the progression of MDD.

1.11 "**Adverse Event**" means the development of an undesirable medical condition or the deterioration of a pre-existing medical condition in a patient or clinical investigation subject following or during exposure to or use of a Compound or Licensed Product, whether or not considered causally related to such Compound or Licensed Product, the exacerbation of any pre-existing condition(s) occurring following or during exposure to or use of such Compound or Licensed Product, or any other adverse experience or adverse drug experience (as described in the FDA's Investigational New Drug safety reporting and NDA post-marketing reporting regulations, 21 C.F.R. §§312.32 and 314.80, respectively, and any applicable corresponding regulations outside the U.S. Territory, in each case as may be amended from time to time), occurring following or during exposure to or use of a Compound or Licensed Product. For purposes of this Agreement, "undesirable medical condition" shall include symptoms (e.g., nausea, chest pain), signs (e.g., tachycardia, enlarged liver) or the abnormal results of an investigation (e.g., laboratory findings, electrocardiogram), including unfavorable side effects, toxicity, injury, overdose or sensitivity reactions.

1.12 "**Affiliate**" means, with respect to any Person, any other Person that, directly or through one or more intermediaries, controls, or is controlled by, or is under common control with, such first Person. For purposes of this definition, "control" means (a) ownership of more than fifty percent (50%) of the shares of stock entitled to vote for the election of directors in the case of a corporation, or more than fifty percent (50%) of the equity interests in the case of any other type of legal entity, (b) status as a general partner in any partnership, or (c) any other arrangement whereby a Person controls or has the right to control the management and policies of such first Person, including via the right to control the board of directors of a corporation or equivalent governing body of an entity other than a corporation.

1.13 "**Agreement**" has the meaning set forth in the preamble hereto.

1.14 "**Alliance Managers**" has the meaning set forth in Section 2.3.1.

1.15 "**Amplixa Annual Global Development Plan**" means each written plan for the Development activities with respect to Compounds and Licensed Products for a Calendar Year prepared and approved pursuant to Section 3.1.1, as the same may be amended, modified or updated in accordance with Section 3.1.1; provided that, for clarity, the first Amplixa Annual Global Development Plan, as agreed as of the Execution Date, shall cover the period from the Effective Date through December 31, 2010.

1.16 "**Amplixa Co-Promotion Information Documents**" has the meaning set forth in Section 3.7.2(a).

1.17 "**Amplixa Global Development Outline**" means the written outline for the Development activities with respect to Compounds and Licensed Products during the Term that, as of the Execution Date, includes Development activities solely with respect to the Primary Compound and Primary Compound Licensed Products and the projected aggregate Initial Development Costs to obtain Regulatory/Pricing Approval for one or more Primary Compound Licensed Products for the Target Indication in the U.S. Territory and the EU.

1.18 "**Amplixa IND**" means IND number **********.

1.19 "**Applicable Laws**" means any federal, state, local, national or supra-national laws, statutes, rules and regulations, including any rules, regulations, guidance, guidelines or requirements of Regulatory Authorities, national securities exchanges, securities listing organizations or patent offices that are in effect from time to time during the Term and applicable to a particular activity hereunder.

1.20 "**AstraZeneca**" has the meaning set forth in the preamble hereto.

1.21 "**AstraZeneca Development Activities**" means the Development activities for one or more Compounds or Licensed Products (a) specified to be conducted by AstraZeneca in any Amplixa Annual Global Development Plan or (b) that the Parties agree in writing shall be conducted by AstraZeneca.

1.22 "********** **Development ********** Right**" has the meaning set forth in Section 3.4.2(a).

1.23 "**AstraZeneca Extended Term Patent Rights**" means, with respect to each Licensed Product in (a) the U.S. Territory, any patents included in the AstraZeneca Patent Rights for which the patent term is extended in the U.S. Territory pursuant to 35 U.S.C. §156 et. seq. or any such future extension or restoration mechanism that may come into force and effect in the U.S. Territory, or (b) each country or jurisdiction in the ROW Territory, such patents included in the AstraZeneca Patent Rights for which the patent term is extended in such country or jurisdiction pursuant to any and all extensions or restorations by existing or future extension or restoration mechanisms (including supplementary protection certificates and the like).

1.24 "**AstraZeneca Indemnitees**" has the meaning set forth in Section 10.1.

1.25 "**AstraZeneca Know-How**" means any Information or Invention owned or Controlled by AstraZeneca or any of its Affiliates on the Execution Date, during the period from the Execution Date until the Effective Date, or during the Term (including, for clarity, as between the Parties, Information discovered, developed or otherwise made during the Term in the conduct of AstraZeneca Development Activities solely by one or more employees of or consultants to AstraZeneca or any of its Affiliates) that is not generally known and that relates to any Compound or Licensed Product and is necessary or reasonably useful, as reasonably determined by AstraZeneca, for Targacept to perform any Targacept Development Activities, but excluding (a) Product Information, (b) Product Invention-Related Information, (c) Joint Program Information, (d) Program Inventions and (e) Inventions claimed or covered by AstraZeneca Patent Rights, AstraZeneca Program Patent Rights or Joint Program Patent Rights.

1.26 "**AstraZeneca Patent Rights**" means all Patent Rights in the entire world owned or Controlled by AstraZeneca or any of its Affiliates as of the Execution Date, during the period from the Execution Date until the Effective Date, or during the Term that claim the composition of matter of, a method of use or Manufacture of, or a pharmaceutical preparation containing or comprising (including the pharmaceutical composition of), or cover the research, development, Manufacture, use, import, offer to sell or sale of, any Compound or Licensed Product, but excluding AstraZeneca Program Patent Rights and Joint Program Patent Rights.

1.27 "**AstraZeneca Program Invention**" means each Program Invention, other than a Product Invention, for which one or more employees of or consultants to AstraZeneca or any of its Affiliates are the sole inventors. Inventorship for purposes of this definition shall be determined by reference to United States patent laws in effect on the Execution Date irrespective of where such Program Invention is actually invented.

1.28 "**AstraZeneca Program Patent Rights**" means all Patent Rights in the entire world that contain one or more claims that cover any AstraZeneca Program Invention.

1.29 "**AstraZeneca Returned Compound**" means, as of any date, any Compound or Licensed Product that either (a) is being Developed or Commercialized in the Territory as of such date or (b) had been Developed or Commercialized in the Territory at any time in the ******** years preceding such date, in each case (clauses (a) and (b)) pursuant to this Agreement.

1.30 "**AstraZeneca Technology**" means, collectively: (a) AstraZeneca Patent Rights; (b) AstraZeneca Know-How; (c) AstraZeneca Program Inventions; (d) AstraZeneca Program Patent Rights; (e) Product Information; and (e) AstraZeneca's interest in Joint Program Information, Joint Program Inventions and Joint Program Patent Rights.

1.31 "**AstraZeneca Termination Technology**" means, as of any date: (a) all Information and Inventions included in AstraZeneca Technology as of such date to the extent actually in use as of such date (or actually used at any time in the ******** years preceding such date) in connection with the Development or Commercialization of any AstraZeneca Returned Compound; and (b) all Patent Rights included in AstraZeneca Technology as of such date to the extent that the Development or Commercialization of any AstraZeneca Returned Compound would infringe such Patent Rights in the absence of a license under such Patent Rights.

1.32 “**AstraZeneca Third Party Agreement**” means any agreement with a Third Party pursuant to which AstraZeneca or any of its Affiliates Controls any AstraZeneca Technology that is the subject of the license granted by AstraZeneca to Targacept pursuant to Section 11.5.1(c) or 11.5.3(c).

1.33 “**Backup R&D Programs**” has the meaning set forth in Section 3.11.1.

1.34 “**Backup R&D Programs Agreement**” has the meaning set forth in Section 3.11.1.

1.35 “**Bankruptcy Code**” has the meaning set forth in Section 11.4.2.

1.36 “**Bayh-Dole Act**” means the Patent and Trademark Law Amendments Act of 1980, as amended, codified at 35 U.S.C. §§200-212, as amended, as well as any regulations promulgated pursuant thereto, including in 37 C.F.R. part 401.

1.37 “**Board of Directors**” has the meaning set forth in the definition of “Change of Control.”

1.38 “**Breaching Party**” has the meaning set forth in Section 11.2.1.

1.39 “**Business Day**” means any day, other than a Saturday or Sunday, on which banking institutions in New York, New York, London, England and Stockholm, Sweden are open for business.

1.40 “**Calendar Quarter**” means each period of three (3) consecutive months ending on the last day of March, June, September or December.

1.41 “**Calendar Year**” means each period of twelve (12) consecutive months from January 1 through December 31.

1.42 “**Chairperson**” has the meaning set forth in Section 2.1.1.

1.43 "**Challenge**" means any challenge to the validity or enforceability of any of the Targacept Patent Rights, Targacept Program Patent Rights or Joint Program Patent Rights, including by: (a) filing a declaratory judgment action in which any of the Targacept Patent Rights, Targacept Program Patent Rights or Joint Program Patent Rights is alleged to be invalid or unenforceable; (b) citing prior art pursuant to 35 U.S.C. §301 or filing a request for re-examination of any of the Targacept Patent Rights, Targacept Program Patent Rights or Joint Program Patent Rights pursuant to 35 U.S.C. §302 or §311 (without the prior written consent of Targacept); (c) provoking or becoming party to an interference with an application for any of the Targacept Patent Rights, Targacept Program Patent Rights or Joint Program Patent Rights pursuant to 35 U.S.C. §135; or (d) filing or commencing any re-examination (without the prior written consent of Targacept), opposition, cancellation, nullity or similar proceedings against any of the Targacept Patent Rights, Targacept Program Patent Rights or Joint Program Patent Rights in any country.

1.44 "**Change of Control**" means, with respect to either Party, the occurrence of any of the following:

(a) any "person" or "group" (as such terms are defined below) (i) is or becomes the "beneficial owner" (as defined below), directly or indirectly, of shares of capital stock or other interests (including partnership interests) of such Party (or any Controlling Affiliate of such Party) then outstanding and normally entitled (without regard to the occurrence of any contingency) to vote in the election of the directors, managers or similar supervisory positions ("**Voting Stock**") of such Party (or its Controlling Affiliate) representing fifty percent (50%) or more of the total voting power of all outstanding classes of Voting Stock of such Party (or its Controlling Affiliate) or (ii) has the power, directly or indirectly, to elect a majority of the members of such Party's (or its Controlling Affiliate's) board of directors or similar governing body (as the case may be, "**Board of Directors**"); or

(b) such Party (or its Controlling Affiliate) enters into a merger, consolidation or other form of business combination, share exchange, reorganization, recapitalization or other similar extraordinary transaction with another Person (whether or not such Party (or its Controlling Affiliate) is the surviving entity) and as a result of such merger, consolidation or other form of business combination, share exchange, reorganization, recapitalization or similar extraordinary transaction (i) the members of the Board of Directors of such Party (or its Controlling Affiliate) immediately prior to such transaction constitute less than a majority of the members of the Board of Directors of such Party (or its Controlling Affiliate) or, if not such Party (or its Controlling Affiliate), such surviving Person immediately following such transaction or (ii) the Persons that beneficially owned, directly or indirectly, the shares of Voting Stock of such Party (or its Controlling Affiliate) immediately prior to such transaction cease to beneficially own, directly or indirectly, shares of Voting Stock representing at least a majority of the total voting power of all outstanding classes of Voting Stock of the surviving Person in substantially the same proportions as their ownership of Voting Stock of such Party (or its Controlling Affiliate) immediately prior to such transaction; or

(c) such Party (or its Controlling Affiliate) sells or transfers to any Third Party, in one or more related transactions, properties or assets representing all or substantially all of the consolidated total assets of such Party and its Affiliates; or

(d) the holders of capital stock of such Party (or its Controlling Affiliate) approve a plan or proposal for the liquidation or dissolution of such Party (or its Controlling Affiliate).

For the purpose of this definition: (x) "person" and "group" have the meanings given such terms under Section 13(d)(3) and 14(d)(2) of the Exchange Act and the term "group" includes any group acting for the purpose of acquiring, holding or disposing of securities within the meaning of Rule 13d-5(b)(1) under the Exchange Act; (y) a "beneficial owner" shall be determined in accordance with Rule 13d-3 under the Exchange Act; and (z) the terms "beneficially owned" and "beneficially own" shall have meanings correlative to that of "beneficial owner".

1.45 "**Claims**" has the meaning set forth in Section 10.1.

1.46 "**Clinical Study**" means a human clinical trial designed to evaluate the safety, efficacy, tolerability or appropriate dosage of a Licensed Product, as the context requires, including Phase 1 Clinical Trials, Phase 2 Clinical Trials, Phase 3 Clinical Trials or Phase 4 Clinical Trials.

1.47 "**Co-Development Activities**" means Targacept Development Activities or AstraZeneca Development Activities, as the case may be.

1.48 "**Co-Development Percentage**" means, with respect to AstraZeneca, eighty percent (80%) and, with respect to Targacept, twenty percent (20%).

1.49 "**Collaboration**" means the alliance of Targacept and AstraZeneca established pursuant to this Agreement.

1.50 "**Combination Product**" means a Licensed Product that is comprised of or contains any Compound as an active pharmaceutical ingredient together with one or more other active pharmaceutical ingredients and is sold either as a fixed dose or as separate doses in a single package.

1.51 “**Commercialization**” or “**Commercialize**” means, with respect to each Licensed Product, any and all lawful activities directed to the commercialization of such Licensed Product, both before and after Regulatory/Pricing Approval of such Licensed Product has been obtained, including activities related to marketing, promoting, detailing, distributing, Manufacturing or having Manufactured (other than Manufacturing Development or Manufacturing for use in Development), importing, selling and offering to sell such Licensed Product, conducting Phase 4 Clinical Trials (other than those required to obtain or maintain Regulatory/Pricing Approval in the U.S. Territory or the EU) and all regulatory affairs activities (including interacting with Regulatory Authorities) regarding any of the foregoing. When used as a verb, “to Commercialize” and “Commercializing” means to engage in Commercialization and “Commercialized” has a corresponding meaning.

1.52 “**Commercially Reasonable Efforts**” means, with respect to:

(a) the performance by Targacept of Targacept Development Activities, efforts and resources consistent in manner and degree with the efforts and resources that ******** for a compound that is at a similar stage of development or market acceptance and with similar technical, safety, medical, regulatory and scientific profiles, characteristics and challenges, a similar level of development and commercialization complexity and difficulty, and a similar potential commercial or strategic value (taking into account stage of research, development or market acceptance, product life, potential financial return, market potential and patent position); or

(b) the performance by AstraZeneca of its obligations with respect to the Development of, seeking Marketing Approval for or the launch or other Commercialization of Licensed Products, efforts and resources consistent in manner and degree with the efforts and resources that ******** for a compound at a similar stage of development or market acceptance and with similar technical, safety, medical, regulatory and scientific profiles, characteristics and challenges, a similar level of development and commercialization complexity and difficulty, and a similar potential commercial or strategic value (taking into account stage of research or development, product life, potential financial return, market potential or share and patent position); provided that, notwithstanding the foregoing, with respect to Developing, seeking Marketing Approval (including, for clarity, Regulatory Approval) for, launching or otherwise Commercializing any particular Licensed Product in any particular Major Country, no ******** of ******** on ******** of ******** or ******** shall be taken into account.

For clarity, (i) in each case (clauses (a) and (b)), Commercially Reasonable Efforts shall be determined on a country-by-country basis, (ii) the application of Commercially Reasonable Efforts requires AstraZeneca to conduct the Initial Development Activities called for by the Amplixa Global Development Outline (beginning on page 4) as agreed as of the Execution Date (as amended or as superseded by an Amplixa Annual Global Development Plan in good faith in a manner that (A) does not reduce such activities or (B) reduces such activities but where such reduced activities remain reasonably expected to be sufficient to obtain Regulatory/Pricing Approval of ******** for the ******** in the ******** and the ********), but excluding Targacept Development Activities, and (iii) without limitation of clause (ii), the application of Commercially Reasonable Efforts may or may not require AstraZeneca to ******** (including, for clarity, ********) for, ******** or otherwise ******** for ******** in ********.

1.53 "**Competitive Activity**" has the meaning set forth in Section 6.1.2(a).

1.54 "**Competitive Product**" has the meaning set forth in Section 6.1.2(b).

1.55 "**Completed Phase 2 Amplixa Study**" means Targacept's completed clinical trial of the Primary Compound (Protocol No. TC-5214-23-CRD-001).

1.56 "**Compound**" means each of (a) the Primary Compound, (b) any ******** of the Primary Compound (including, for clarity, the ******** Compound), (c) any prodrug, ester, salt, polymorph, hydrate or solvate of either of the foregoing (clauses (a) or (b)), and (d) any compound that all of:

(i) has any of ******** and ******** set forth on Schedule 11 attached hereto;

(ii) has no ******** at any ********; and

(iii) acts as a ******** (showing ******** of ******** at a concentration of such compound below ********) of either:

(A) each of the same ******** at which the Primary Compound acts as a ******** (showing ******** of ******** at a concentration of the Primary Compound below ********); or

(B) both (1) each of the ******** or ******** and (2) either of the ******** or ********.

For clarity, the ******** identified on Schedule 11 include simple ********, and simple ********, including ******** and all ******** of the foregoing (including, for clarity, any ********).

1.57 "**Confidential Information**" has the meaning set forth in Section 8.2.1.

1.58 "**Consensus Patent-Related Matter**" has the meaning set forth in Section 7.5.1.

1.59 "**Consensus Patent Rights**" has the meaning set forth in Section 7.7.2(a).

1.60 "**Control**," "**Controls**," "**Controlled**" **or** "**Controlling**" means (a) with respect to Information, Inventions, Patent Rights or other intellectual property rights (other than Proprietary Materials), possession of the legal right (other than pursuant to the licenses granted under Section 4.1.1 or Section 4.1.2, as applicable) to grant the licenses or sublicenses under such Information, Inventions, Patent Rights or other intellectual property rights provided herein, in each case if applicable, without violating the terms of any agreement or other arrangement with any Third Party and (b) with respect to Proprietary Materials, the possession by a Party of the right to supply such Proprietary Materials to the other Party as provided herein without violating the terms of any agreement or arrangement with any Third Party. A Party shall be deemed to Control Joint Program Information, Joint Program Inventions or Joint Program Patent Rights to the extent of its individual or joint interest therein, as applicable.

1.61 "**Controlling Affiliate**" means, with respect to any Party or other Person, an Affiliate of such Party or other Person that controls (within the meaning given under the definition of "Affiliate") such Party or other Person.

1.62 "**Cooperating Party**" has the meaning set forth in Section 7.12.4.

1.63 "**Co-Promoted Products**" means Licensed Products, but only if Targacept has exercised its Co-Promotion Right and thereafter for so long as the Co-Promotion Agreement remains in effect.

1.64 "**Co-Promotion Agreement**" has the meaning set forth in Section 3.10.1.

1.65 "**Co-Promotion Right**" has the meaning set forth in Section 3.10.

1.66 "**Cost Audited Party**" and "**Cost Auditing Party**" have the respective meanings set forth in Section 3.9.2(b).

1.67 "**CREATE Act**" has the meaning set forth in Section 7.11.

1.68 “**Develop**” or “**Development**” means any and all activities that relate to (a) the research and development of any Compound or Licensed Product (other than Phase 4 Clinical Trials, unless required to obtain or maintain Regulatory/Pricing Approval in the U.S. Territory or the EU) and (b) obtaining, or that are required to maintain, Regulatory/Pricing Approval of Licensed Products in the Territory. Development includes Preclinical Activities, pharmacology studies, biomarker studies, toxicology studies, DMPK studies, Manufacturing Development, Manufacturing or having Manufactured for use in Development, quality assurance and quality control, technical support, pharmacokinetic studies, Clinical Studies (other than Phase 4 Clinical Trials, unless required to obtain or maintain Regulatory/Pricing Approval in the U.S. Territory or the EU), preparing and filing Drug Approval Applications and all regulatory affairs activities (including interacting with Regulatory Authorities) regarding any of the foregoing. When used as a verb, “Developing” means to engage in Development and “Developed” has a corresponding meaning.

1.69 “**Development Cost Reconciliation Report**” has the meaning set forth in Section 3.9.2(a).

1.70 “**Development Costs**” means, with respect to each Compound or Licensed Product, the reasonable out-of-pocket costs, internal costs of a Party or any of its Affiliates, and costs with respect to the supply of such Compound or Licensed Product (including placebos) for use in Clinical Studies, in each case that are incurred after the Effective Date and that are both specifically attributable to the Development of such Compound or Licensed Product and generally consistent with such Party’s Co-Development Activities as specified in the then-current Amplixa Annual Global Development Plan. For purposes of this definition and subject to the conditions set forth above: (a) “out-of-pocket costs” means, with respect to each Compound or Licensed Product, actual amounts paid to a Third Party, including all license fees (excluding any payments to a Third Party under the Targacept Sublicense Agreements) and filing fees required for, and other costs associated with, any Regulatory Filings applicable to such Compound or Licensed Product; (b) “internal costs” means the applicable FTE Rate(s) multiplied by the actual number of FTEs utilized; (c) with respect to each Clinical Study, unless otherwise agreed by the Parties, in no event shall the internal costs incurred by a Party for such Clinical Study, excluding costs with respect to the supply of the applicable Compound or Licensed Product (including placebos) for use in such Clinical Study, exceed ******** (*********%) of the out-of-pocket costs incurred by such Party therefor; and (d) costs with respect to the supply of the applicable Compound or Licensed Product (including placebos) for use in Clinical Studies means (i) if such Compound or Licensed Product (or placebo) is purchased from a Third Party, the actual costs paid by AstraZeneca or Targacept to such Third Party with respect to such Compound or Licensed Product (or placebo), or (ii) if such Compound or Licensed Product (or placebo) is Manufactured by AstraZeneca or any of its Affiliates, AstraZeneca’s (or its Affiliate’s) fully burdened (determined as provided on Schedule 10 attached hereto) costs for Manufacturing such Compound or Licensed Product (or placebo).

1.71 “**Development Liaison**” has the meaning set forth in Section 2.3.2.

1.72 “**Development Program**” means the Development program to be conducted by the Parties during the Term pursuant to the Amplixa Annual Global Development Plans to obtain Regulatory/Pricing Approval of one or more Licensed Products in the Territory.

1.73 “**Development Regulatory Filing**” means, with respect to each Compound or Licensed Product: each (a) NDA or other Drug Approval Application; (b) IND; (c) application for “Fast Track” status under Section 506 of the FDCA (21 U.S.C. §356) or for a Special Protocol Assessment under Section 505(b)(4)(B) and (C) of the FDCA (21 U.S.C. §355(b)(4)(B) and §355(b)(4)(C)) or the analogous application or request with respect to Major Countries outside the U.S. Territory; in each case (clauses (a), (b) and (c)) with respect to such Compound or Licensed Product in Major Countries (including, for clarity, via the centralized procedure in the EU); and (d) all supplements and amendments to any of the foregoing.

1.74 “**Development Working Group**” has the meaning set forth in Section 2.2.

1.75 “**Disclosing Party**” has the meaning set forth in Section 8.2.2.

1.76 “**Dispute**” has the meaning set forth in Section 12.1.1.

1.77 “**Distributor**” has the meaning set forth in Section 4.5.

1.78 “**Dollars**” means U.S. dollars.

1.79 “**Drug Approval Application**” means, with respect to each Licensed Product in a particular country or jurisdiction, an application to commercially distribute, sell or market such Licensed Product in such country or jurisdiction, including: (a) an NDA or sNDA; (b) the analogous application to an NDA or sNDA in any country or jurisdiction in the ROW Territory; and (c) all supplements and amendments to any of the foregoing.

1.80 “**DSM IV**” means the Diagnostic and Statistical Manual of Mental Disorders, Fourth Edition, published by the American Psychiatric Association (text revision, 2000), as amended and as supplemented or superseded by subsequent editions published from time to time.

1.81 “**Effective Date**” has the meaning set forth in Section 12.19.3.

1.82 "**Election Period**" has the meaning set forth in Section 12.5.2(a).

1.83 "**EMEA**" means the European Medicines Agency or, as used in any particular context hereunder, any successor thereto for the purpose contemplated in such context.

1.84 "**End of Phase 2 Meeting**" means any meeting with the FDA for the purpose of (a) reviewing data from a Phase 2 Clinical Trial for a Licensed Product or (b) discussing the design of a pivotal Phase 3 Clinical Trial for a Licensed Product.

1.85 "**European Union**" or "**EU**" means Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, The Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom, and any such other country or territory that may officially become part of the European Union after the Execution Date.

1.86 "**Excepted Decision**" has the meaning set forth in Section 2.1.5(a).

1.87 "**Excess Additional Development Costs Offset**" has the meaning set forth in Section 5.11.2.

1.88 "**Excess Initial Development Costs Offset**" has the meaning set forth in Section 5.11.1.

1.89 "**Exchange Act**" means the Securities Exchange Act of 1934, as amended.

1.90 "**Excluded Indications**" means the management, treatment, prevention, cure or delayed progression of hypertension, in any form and however caused.

1.91 "**Exclusivity Period**" has the meaning set forth in Section 6.1.1.

1.92 "**Execution Date**" has the meaning set forth in the preamble hereto.

1.93 "**Executive Officers**" has the meaning set forth in Section 2.1.5(a).

1.94 "**Existing CDA**" means that certain Confidentiality Agreement between AstraZeneca Pharmaceuticals LP and Targacept dated December 3, 2008, as amended.

1.95 "**Existing Patent Rights**" means the Targacept Patent Rights set forth on Part A, Part B and Part C, collectively, of Schedule 2 attached hereto.

1.96 "**Existing Trademarks**" means the Trademarks listed on Schedule 3 attached hereto.

1.97 "**Existing TRGT Alliance Agreement**" means the Product Development and Commercialization Agreement by and between SmithKline Beecham Corporation (d/b/a GlaxoSmithKline) and Glaxo Group Limited, on the one hand, and Targacept, on the other hand, dated July 27, 2007, as may be amended from time to time.

1.98 "**Existing TRGT API Agreements**" and "**Existing TRGT Supply Agreement**" have the respective meanings set forth in Section 3.3.2.

1.99 "**Expanded Field Indication**" has the meaning set forth in Section 4.7.2.

1.100 "**Experts**" has the meaning set forth in Section 12.1.2(a).

1.101 "**FDA**" means the U.S. Food and Drug Administration or, as used in any particular context hereunder, any successor thereto for the purpose contemplated in such context.

1.102 "**FDCA**" means the United States Federal Food, Drug, and Cosmetic Act, as amended.

1.103 "**Field**" means any and all uses, excluding the Excluded Indications; provided that, if under the circumstances set forth in Section 4.7.2 AstraZeneca has an option to expand the Field to include an Excluded Indication and exercises such option, "Field" shall include such Excluded Indication from and after such exercise.

1.104 "**First Commercial Sale**" means, with respect to each Licensed Product and each country or jurisdiction, the first sale of such Licensed Product for use or consumption by the general public in such country or jurisdiction after: (a) Regulatory Approval from the applicable Regulatory Authority has been obtained; and (b) solely in the case of ******** or ******** is ********, (i) such ******** or ******** from the applicable Regulatory Authority has been obtained or (ii) solely with respect to Section 5.2.1 (and, for clarity, not for purposes of determining a Royalty Term or for any other purpose), such ******** or ******** from the applicable Regulatory Authority has not been obtained but ******** of such Licensed Product as an ******** in ********, as a ******** in ******** or as either an ******** or a ******** in ********, as applicable, are ********; provided that a sale of a Licensed Product to a Party's Affiliate or Sublicensee shall not constitute a First Commercial Sale (unless the purchasing Affiliate or Sublicensee is the last Person in the distribution chain for such Licensed Product and is purchasing it for its own commercial use). For clarity, sales prior to satisfaction of clause (a) and, if applicable, clause (b)(i) above, such as so-called "treatment IND sales," "named patient sales" and "compassionate use sales" shall not be construed as a First Commercial Sale.

1.105 "**Force Majeure**" means an event that is beyond a non-performing Party's reasonable control, including an act of God, act of the other Party, strike, lock-out or other industrial/labor dispute (whether involving the workforce of the non-performing Party or of any other Person), war, riot, civil commotion, terrorist act, malicious damage, epidemic, quarantine, fire, flood, storm, natural disaster, or compliance with any injunction, law, order, proclamation, regulation, ordinance, demand or requirement of any government or of any subdivision, authority or representative of any such government (including changes in the requirements of a Regulatory Authority), whether or not it is later held to be invalid, except to the extent any such injunction, law, order, proclamation, regulation, ordinance, demand or requirement operates to delay or prevent the non-performing Party's performance as a result of any breach by such Party or any of its Affiliates of any term or condition (including any representation or warranty) of this Agreement, the Co-Promotion Agreement (if any) or the Backup R&D Programs Agreement (if any).

1.106 "**FTE**" means ************ and ************ hours of work devoted to or in support of Development of Compounds or Licensed Products in accordance with an Amplixa Annual Global Development Plan that is carried out by one or more employees or temporary contract personnel of a Party, measured in accordance with such Party's normal time allocation practices from time to time, consistently applied.

1.107 "**FTE Cost**" means, for any period, the applicable FTE Rate multiplied by the number of FTEs in such period.

1.108 "**FTE Rate**" means a rate of ************ Dollars (US $************) per FTE per annum; provided that on January 1 of each Calendar Year in the Term, commencing with January 1, 2011, the FTE Rate will be increased by multiplying the FTE Rate applicable on December 31 of the immediately preceding Calendar Year by 1 + [(CPIx - CPIy) / CPIy], where CPIx is the United States Consumer Price Index for All Urban Consumers (1982-84=100) published by the Bureau of Labor Statistics of the United States Department of Labor for December in the immediately preceding Calendar Year and CPIy is the United States Consumer Price Index for All Urban Consumers (1982-84=100) published by the Bureau of Labor Statistics of the United States Department of Labor for the month immediately preceding the Effective Date. Any such increase shall be rounded to the nearest one hundred Dollars (US $100).

1.109 "**GLP**" means the then-current requirements under Applicable Laws for nonclinical laboratory studies that support or are intended to support applications to conduct research in humans or to obtain marketing authorization, including as set forth in 21 C.F.R. part 58 and EC Directives 87/18/EEC, 88/320/EEC and 1999/11/EC, and as otherwise required by the Regulatory Authorities of the EU, the United States and Japan, in each case as amended from time to time.

1.110 "**Good Clinical Practices**" means the then-current requirements under Applicable Laws and international ethical, scientific and quality standards for designing, conducting, recording, analyzing and reporting trials that involve the participation of human subjects, including as set forth in 21 C.F.R. parts 50, 54, 56 and 312 and in the International Conference on Harmonization Guideline for Good Clinical Practice (E6), in each case as amended from time to time.

1.111 "**Good Manufacturing Practices**" means the then-current requirements under Applicable Laws for the manufacturing, preparation, processing, labeling, packaging, and distribution of pharmaceutical products (and components thereof), including as set forth in 21 U.S.C. Section 351, 21 C.F.R. parts 210 and 211, European Commission Directive 2003/94/EEC of 08 October 2003, and as otherwise required by the Regulatory Authorities of the EU, the United States and Japan, in each case as amended from time to time.

1.112 "**Hatch-Waxman Act**" means the Drug Price Competition and Patent Term Restoration Act of 1984, as amended.

1.113 "**HSR Act**" means the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 U.S.C. §18a), as amended.

1.114 "**IND**" means an investigational new drug application submitted to the FDA pursuant to 21 C.F.R. part 312, including any supplements and amendments thereto. References herein to IND shall include, to the extent applicable, any analogous Regulatory Filing in the ROW Territory (including a Clinical Trial Authorization in the European Union).

1.115 "**Indemnification Claim Notice**" has the meaning set forth in Section 10.3.1.

1.116 "**Indemnified Party**" and "**Indemnifying Party**" have the respective meanings set forth in Section 10.3.1.

1.117 "**Indemnitees**" has the meaning set forth in Section 10.3.1.

1.118 "**Indication**" means any human disease or condition that can be treated, prevented, cured or the progression of which can be delayed.

1.119 "**Indirect Taxes**" means value added taxes, sales taxes, consumption taxes and other similar taxes.

1.120 "**Information**" means all tangible and intangible information, techniques, trade secrets, technical information, methods, processes, know-how, data and results (including pharmacological, toxicological and clinical test data and results and market research or commercial data), analytical and quality control data, laboratory notes and notebooks, results or descriptions. Notwithstanding the foregoing, Information does not include Inventions.

1.121 "**Infringement**" and "**Infringement Notice**" have the respective meanings set forth in Section 7.12.1(a).

1.122 "**Initiation**" or "**Initiate**" means, with respect to a Clinical Study, the first dosing of the first subject in such Clinical Study, unless AstraZeneca has made an affirmative determination reasonably and in good faith, and so informed Targacept, that it is more likely than not that such subject should not have been enrolled in such Clinical Study for failure to meet the subject selection criteria outlined in the applicable protocol.

1.123 "**Initial Development Activities**" has the meaning set forth in the Amplixa Global Development Outline as agreed as of the Execution Date.

1.124 "**Initial Development Costs**" means all Development Costs with respect to Initial Development Activities.

1.125 "**Initial Notice Deadline**" has the meaning set forth in Section 3.9.1(b)(ii).

1.126 "**In-Licensed Patent Rights**" has the meaning set forth in Section 9.2.3.

1.127 "**Invention**" means any new or useful process, composition of matter, formulation, design, device, kit or method of use or manufacture that is reasonably expected to be patentable under Applicable Laws (whether or not patented), as determined pursuant to Section 7.5.

1.128 "**Joint Development Committee**" or "**JDC**" has the meaning set forth in Section 2.1.

1.129 "**Joint Program Information**" means all Program Information discovered, developed or otherwise made jointly by one or more employees of or consultants to Targacept or any of its Affiliates, on the one hand, and one or more employees of or consultants to AstraZeneca or any of its Affiliates, on the other hand, but excluding Product Information and Product Invention-Related Information.

1.130 "**Joint Program Invention**" means each Program Invention, other than a Product Invention, for which one or more employees of or consultants to AstraZeneca or any of its Affiliates, on the one hand, and one or more employees of or consultants to Targacept or any of its Affiliates, on the other hand, are inventors. Inventorship for purposes of this definition shall be determined by reference to United States patent laws in effect on the Execution Date irrespective of where such Program Invention is actually invented.

1.131 "**Joint Program Patent Rights**" means all Patent Rights in the entire world that contain one or more claims that cover any Joint Program Invention.

1.132 "**Knowledge**" means, subject to Section 12.15, the good faith understanding and awareness of the facts and information by: (a) with respect to each Party, ******** of such Party or any of its Affiliates, or any ******** of, or ******** by, such Party or any of its Affiliates; and (b) with respect to Targacept, ******** or ******** in each case (clauses (a) and (b)) without any duty to conduct any investigation with respect to such facts and information by reason of the execution of this Agreement or the formation of the Collaboration. For purposes of this definition, ******** means any individual in the position of ******** or ********. "**Known**" has the corresponding meaning.

1.133 "**Lead Compound**" means the Primary Compound unless the Primary Compound is not the most advanced Compound in Development or being Commercialized in the Collaboration, in which case "Lead Compound" means the most advanced Compound in Development or being Commercialized in the Collaboration.

1.134 "**LIBOR**" means the London Interbank Offered Rate for deposits in Dollars having a maturity of one (1) month published by the British Bankers' Association, as adjusted from time to time on the first (1st) London business day of each month.

1.135 "**Licensed Product**" means each pharmaceutical or medicinal item, substance or formulation that is comprised of or contains any Compound, whether or not the sole active pharmaceutical ingredient. For clarity, Licensed Products include Combination Products.

1.136 "**Losses**" has the meaning set forth in Section 10.1.

1.137 "**MADRS**" means the Montgomery-Asberg Depression Rating Scale.

1.138 "**Major Country**" means each of ********.

1.139 "**Manufacture**" or "**Manufacturing**" or "**Manufactured**" means all operations involved in the manufacture, receipt, incoming inspections, storage and handling of Materials, and the manufacture, processing, purification, formulation, packaging, labeling, warehousing, quality control testing (including in-process release and stability testing), quality assurance, shipping and release of any Compound or Licensed Product.

1.140 “**Manufacturing Development**” means all activities related to the optimization of a commercial-grade Manufacturing process for the Manufacture of any Compound or Licensed Product, including test method development and stability testing, formulation, validation, productivity, trouble shooting and second generation formulation, process development, Manufacturing scale-up, development-stage Manufacturing, and quality assurance/ quality control development.

1.141 “**Marketing Approval**” means, with respect to each Licensed Product and each country or jurisdiction, all approvals, licenses, registrations or authorizations of Regulatory Authorities necessary or reasonably useful to commercially distribute, sell, or market such Licensed Product in such country or jurisdiction, including Regulatory/Pricing Approval.

1.142 “**Materials**” means all raw materials, including Compound, intermediates, solvents, reactants, excipients, components, containers, labels and packaging materials necessary for the Manufacture of any Compound or Licensed Product.

1.143 “**MDD**” means major depressive disorder as described in DSM IV from time to time. For clarity, as of the Execution Date, MDD is as encoded in DSM IV as 296.2x or 296.3x.

1.144 “**MHLW**” means the Ministry for Health, Labor and Welfare of Japan or the Pharmaceutical and Medical Devices Agency (the “**PMDA**,” formerly known as IYAKUHIN SOGO KIKO), or, as used in any particular context hereunder, any successor to either of them, as the case may be, for the purpose contemplated in such context.

1.145 “**Milestone Event**” means each of the events identified as a milestone event in Section 5.2.1 or Section 5.2.2.

1.146 “**Milestone Product**” has the meaning set forth on Schedule 4 attached hereto.

1.147 “**Monotherapy**” means, with respect to a Licensed Product, that such Licensed Product is any of (a) labeled for use, (b) the subject of a Drug Approval Application for approval to be labeled for use or (c) the subject of a Phase 3 Clinical Trial for evaluation, in each case (clauses (a), (b) and (c)) by itself, without any other pharmaceutical product, to treat, prevent, cure or delay the progression of MDD.

1.148 “**NCB**” means any compound that both: (a) blocks the channel of an NNR as a principal mechanism of action; and (b) does not occupy the site at which acetylcholine naturally accesses such NNR (commonly referred to as “binding”).

1.149 “**NDA**” means a New Drug Application (as more fully described in Title 21 of the U.S. Code of Federal Regulations, Section 314.50) filed with the FDA, or any successor application in the U.S. Territory.

1.150 “**Net Sales**” means, with respect to each Licensed Product, the gross invoiced sales price of such Licensed Product sold by AstraZeneca or any of its Affiliates, Sublicensees or Net Sales Distributors (each, a “**Selling Party**”) in finished product form, packaged and labeled for sale, to Third Parties (including Distributors, but, for clarity, not Net Sales Distributors), less deductions allowed by the Selling Party and incurred, allowed, paid, accrued or specifically allocated in its financial statements in accordance, where applicable, with International Financial Reporting Standards (“**IFRS**”) for any Selling Party that accounts in accordance with IFRS or generally accepted accounting principles in the United States (“**GAAP**”) for any Selling Party that accounts in accordance with GAAP, in each case applied on a consistent basis, for:

(a) normal and customary trade, quantity or prompt settlement discounts (including chargebacks and allowances);

(b) administration, service, inventory management or similar fees paid to a wholesaler, distributor, group purchasing organization, buying group, or similar organization pursuant to a contract between the Selling Party and such wholesaler, distributor, group purchasing organization, buying group, or similar organization, relating to the sale of Licensed Products by the Selling Party;

(c) credits, rebates, or discounts made to or for the account of a customer or a payor pursuant to a contract between the Selling Party and such customer or payor, relating to the sale of Licensed Products by the Selling Party to such customer or for the account of such payor;

(d) rebates, discounts, credits, price concessions, and other payments made with respect to sales paid for, or required as a condition of participation in or reimbursement under, any program administered or funded from time to time during the Term by any governmental or regulatory authority, including Federal or state Medicaid, Medicare or similar state program in the U.S. Territory or equivalent governmental program in any other country, including any rebates, discounts, credits, price concessions, and other payments that may be required by any healthcare reform legislation or other Applicable Laws that may be enacted or promulgated after the Execution Date;

(e) ******** or ******** on account of ******** or ******** (including ******** and ********) or on account of bona fide ******** affecting such Licensed Product;

(f) sales (such as VAT or its equivalent) and excise taxes, other consumption taxes, customs duties and compulsory payments to governmental authorities and any other governmental charges imposed upon the importation, use or sale of such Licensed Product to Third Parties (excluding any taxes paid on the income from such sales), to the extent the Selling Party is not otherwise entitled to a credit or a refund for such taxes, duties or payments made;

(g) ******** related to ******** or ******** provided by the Selling Party to ********, or other ******** through ********, or ********;

(h) actual ******** (i.e., when such ******** is no longer recorded as a ********) specifically attributable to such Licensed Product;

(i) any other similar deductions that are ******** as of the ******** but ******** in the ******** after the ********; and

(j) ********.

Sales of a Licensed Product between AstraZeneca and its Affiliates, Sublicensees or Net Sales Distributors shall be excluded from the computation of Net Sales, except where any such Affiliate, Sublicensee or Net Sales Distributor is the last Person in the distribution chain for such Licensed Product and is purchasing it for its own commercial use. In addition, no Licensed Product provided to patients for compassionate use, as "treatment IND sales" or as "named patient sales" shall be included in Net Sales.

In the case of pharmacy incentive programs, hospital performance incentive programs, chargebacks, disease management programs, or any similar programs or discounts on portfolio product offerings, all rebates, discounts and other forms of reimbursements shall be allocated among products on the basis on which such rebates, discounts and other forms of reimbursements were actually granted or, if such basis cannot be determined, in accordance with the Selling Party's existing allocation method; provided, however, that any such allocation shall be reasonable, consistent and done in strict accordance with Applicable Laws, including any price reporting laws, rules and regulations.

In the event that a Licensed Product is sold in any country in the form of a Combination Product, Net Sales of such Combination Product shall be adjusted by multiplying actual Net Sales of such Combination Product in such country calculated pursuant to the foregoing definition of "Net Sales" by the fraction A/(A+B), where A is the average invoice price in such country of any Licensed Product that contains the applicable Compound as its sole active pharmaceutical ingredient, if sold separately in such country, and B is (i) except as provided in clause (ii) below, the average invoice price(s) in such country of each product(s) that contains an active pharmaceutical ingredient other than the Compound contained in such Combination Product as its sole active pharmaceutical ingredient, if sold separately in such country, or (ii) where an active pharmaceutical ingredient other than the Compound contained in such Combination Product is an active pharmaceutical ingredient that is a **********, the lesser of (A) the amount in clause (i) above or (B) the actual cost to the Selling Party to make or obtain such active pharmaceutical ingredient (or, for clarity, the product that contains such active pharmaceutical ingredient) for inclusion in such Combination Product. If either such Licensed Product that contains such Compound as its sole active pharmaceutical ingredient or, solely in the case of clause (i) above, a product that contains an active pharmaceutical ingredient (other than such Compound) in the Combination Product is not sold separately in a particular country, the Parties shall negotiate in good faith a reasonable adjustment to Net Sales in such country that takes into account the medical contribution to the Combination Product of, and all other factors reasonably relevant to the relative value of, the applicable Compound, on the one hand, and all of the other active pharmaceutical ingredients, collectively, on the other hand; provided that if, notwithstanding such good faith negotiation, the Parties are unable to agree on an adjustment to Net Sales in such country within ********** days after a request by a Party that they negotiate such an adjustment, then either Party shall have the right to submit such matter for resolution pursuant to Section 12.1.

For purposes of the immediately preceding paragraph, the invoice price in a country for each Licensed Product that contains only a Compound and each product that contains solely active pharmaceutical ingredients other than the Compound included in the Combination Product shall be for a quantity comparable to that used in such Combination Product and of substantially the same class, purity and potency.

The Parties agree that, in the event that either Party proposes that this definition of Net Sales be amended to reflect changes required by the adoption of new accounting standards applicable to such Party, whether due to a Change of Control or a requirement of Applicable Laws, the other Party shall consider such proposal reasonably and in good faith.

1.151 "**Net Sales Distributor**" has the meaning set forth in Section 4.5.

1.152 "**NNR**" means a neuronal nicotinic receptor.

1.153 "**NNR Subtype**" means, a particular collection of protein subunits that, when combined in a specific pentameric manner, form a functional NNR.

1.154 "**Non-Breaching Party**" has the meaning set forth in Section 11.2.1.

1.155 "**Non-Consensus Targacept Program Patent Rights**" has the meaning set forth in Section 7.7.2(b)(iii).

1.156 "**********" Application" means the patent application set forth under such heading in Part C of Schedule 2 attached hereto.

1.157 "**Orange Book**" means the publication Approved Drug Products with Therapeutic Equivalence Evaluations that identifies drug products approved on the basis of safety and effectiveness by the FDA under the FDCA.

1.158 "**Owned Patent Rights**" has the meaning set forth in Section 9.2.3.

1.159 "**Party**" or "**Parties**" has the meaning set forth in the preamble hereto.

1.160 "**Patent Coordinator**" has the meaning set forth in Section 7.4.

1.161 "**Patent Costs**" means the reasonable fees and expenses paid to outside legal counsel, and filing, maintenance and other reasonable out-of-pocket expenses paid to Third Parties, in connection with the Prosecution and Maintenance of Patent Rights.

1.162 "**Patent-Related Matter**," "**Patent-Related Matter Deadline**" and "**Patent-Related Matter Resolution Deadline**" have the respective meanings set forth in Section 7.5.1.

1.163 “**Patent Rights**” means: (a) all national, regional and international patents and patent applications, including provisional patent applications; (b) all patent applications filed either from a patent or patent application described in clause (a) or from an application claiming priority to a patent or patent application described in clause (a), including divisionals, continuations, continuations-in-part, provisionals, converted provisionals, and continued prosecution applications; (c) any and all patents that have issued or in the future issue from the foregoing patent applications (clauses (a) and (b)), including utility models, petty patents and design patents and certificates of invention; (d) any and all extensions or restorations by existing or future extension or restoration mechanisms, including revalidations, reissues, re-examinations and extensions (including any supplementary protection certificates and the like) of the foregoing patents or patent applications (clauses (a), (b) and (c)); and (e) any similar rights, including so-called pipeline protection, or any importation, revalidation, confirmation or introduction patent or registration patent or patent of additions to any such foregoing patent applications and patents.

1.164 “********** Agreement**” has the meaning set forth in Section 3.3.2.

1.165 “**Payments**” has the meaning set forth in Section 5.9.

1.166 “**Person**” means an individual, sole proprietorship, partnership, limited partnership, limited liability partnership, corporation, limited liability company, business trust, joint stock company, trust, incorporated association, joint venture or similar entity or organization, including a government or political subdivision, department or agency of a government.

1.167 “**Phase 1 Clinical Trial**” means a human clinical trial of a pharmaceutical product candidate, in healthy volunteers or patients, that generally provides for the first introduction into humans of such product candidate, with the principal purpose of obtaining data regarding any or all of the safety, metabolism, pharmacokinetic properties and clinical pharmacology, and potentially early evidence on effectiveness, of such product candidate, as described or contemplated by 21 C.F.R. §312.21(a).

1.168 “**Phase 2 Clinical Trial**” means a human clinical trial, following completion of one or more Phase 1 Clinical Trials, of a pharmaceutical product candidate in subjects with a particular disease or condition, with a principal purpose of evaluating the effectiveness, safety, and acceptable dose range for such product candidate for a particular use, as described or contemplated by 21 C.F.R. §312.21(b).

1.169 "**Phase 3 Clinical Trial**" means a human clinical trial of a pharmaceutical product candidate in subjects with a particular disease or condition that is designed to establish that such product candidate is safe and efficacious for its intended use so as to support Regulatory Approval of such product candidate, as described or contemplated by 21 C.F.R. §312.21(c); provided that it is not intended that a human clinical trial must, by itself, support Regulatory Approval of a product candidate (including, for clarity, itself establish that such product candidate is safe and efficacious for its intended use) in order to be a Phase 3 Clinical Trial.

1.170 "**Phase 4 Clinical Trial**" means a human clinical trial of a pharmaceutical product for a particular Indication and patient population, after receipt of Regulatory Approval for such Indication and patient population, whether or not such clinical trial is required to be conducted as a condition to obtaining or maintaining such Regulatory Approval. For clarity, for purposes of this Agreement, a human clinical trial designed to support an expansion of the patient population for which a particular Licensed Product is labeled for use in the U.S. Territory or the EU is not a Phase 4 Clinical Trial; provided that a human clinical trial designed to support the modification of a label to include expressly a subset of the patient population for which a particular Licensed Product is already labeled for use is a Phase 4 Clinical Trial. For clarity and notwithstanding the foregoing, any human clinical trial of a pharmaceutical product for a particular Indication, after receipt of Regulatory Approval for such Indication, that is not required by the applicable Regulatory Authority to maintain such Regulatory Approval (or to obtain Regulatory Approval in another country in the Territory) and that AstraZeneca reasonably determines to be a Phase 4 Clinical Trial shall, for purposes of this Agreement, be a Phase 4 Clinical Trial.

1.171 "**Preclinical Activities**" means in vitro and in vivo animal studies, not in humans, including those studies conducted in whole animals and other test systems, designed to determine any or all of the toxicity, bioavailability, pharmacokinetics and other pharmacological properties of a compound, as described or contemplated by 21 C.F.R. §58.3(d).

1.172 "**Primary Compound**" means the pharmaceutical compound described on Schedule 1 attached hereto known by Targacept as of the Execution Date as TC-5214 or Amplixa™.

1.173 "**Primary Compound Licensed Product**" means each Licensed Product that is comprised of or contains the Primary Compound.

1.174 "**Product Information**" means all Program Information that relates solely to one or more Compounds or Licensed Products, but excluding Product Invention-Related Information.

1.175 "**Product Invention**" means (a) each Program Invention that has ******** one or more Compounds or Licensed Products or the use of one or more Compounds or Licensed Products, but excluding any Program Invention that constitutes a ******** or ******** or ********, and (b) each Program Invention that constitutes a ******** or ******** or ******** that ******** one or more Compounds or Licensed Products or ******** one or more Compounds or Licensed Products.

1.176 "**Product Invention-Related Information**" means, with respect to each Product Invention, all Program Information that has ******** such Product Invention, including any applicable Information contained in laboratory notebooks or other documentation establishing inventorship or demonstrating conception or reduction to practice.

1.177 "**Product Regulatory Approval**" means each approval, license, registration or authorization included in Marketing Approval.

1.178 "**Product Trademark**" means, with respect to each Licensed Product, each Trademark, whether or not registered, or trademark application or renewal, extension or modification thereof, under which such Licensed Product is marketed in the Territory, together with all goodwill associated therewith and promotional materials relating thereto. For purposes of clarity, Product Trademarks shall not include any name or logo used by AstraZeneca or any of its Affiliates that is not specific to a Licensed Product.

1.179 "**Program Information**" means all Information that is discovered, developed or otherwise made in connection with the Development or Commercialization of Compounds or Licensed Products (i) solely by one or more employees of or consultants to Targacept or any of its Affiliates, (ii) solely by one or more employees of or consultants to AstraZeneca or any of its Affiliates or (iii) jointly by one or more employees of or consultants to Targacept or any of its Affiliates, on the one hand, and one or more employees of or consultants to AstraZeneca or any of its Affiliates, on the other hand.

1.180 "**Program Invention**" means each Invention (a) that is invented in connection with the Development or Commercialization of any Compound or Licensed Product and (b) for which (i) one or more employees of or consultants to Targacept or any of its Affiliates are inventors, (ii) one or more employees of or consultants to AstraZeneca or any of its Affiliates are inventors, or (iii) one or more employees of or consultants to Targacept or any of its Affiliates, on the one hand, and one or more employees of or consultants to AstraZeneca or any of its Affiliates, on the other hand, are inventors. Inventorship for purposes of this definition shall be determined by reference to United States patent laws in effect on the Execution Date irrespective of where such Invention is actually invented.

1.181 "**Proprietary Materials**" means tangible chemical, biological or physical materials that are furnished by or on behalf of one Party to the other Party in connection with this Agreement and are not generally available or accessible from sources other than the furnishing Party, whether or not specifically designated as proprietary by the furnishing Party.

1.182 "**Prosecution and Maintenance**" or "**Prosecute and Maintain**" means, with regard to particular Patent Rights, the preparing, filing, prosecuting and maintenance of such Patent Rights, as well as re-examinations and reissues with respect to such Patent Rights, together with the conduct of interferences, the defense of oppositions and other similar proceedings with respect to such Patent Rights. For clarity, "Prosecution and Maintenance" or "Prosecute and Maintain" shall not include any other enforcement action taken with respect to Patent Rights.

1.183 "**********" means a Licensed Product that is an Adjunct Therapy or a Monotherapy in ********** containing ********** Primary Compound as its sole active pharmaceutical ingredient.

1.184 "********** **Initial Development Cost Maximum**" means aggregate Development Costs incurred by the Parties with respect to one or more ********** equal to the lesser of (a) ********** Dollars ($**********) or (b) the amount of aggregate Development Costs incurred by the Parties with respect to all ********** in the aggregate as of the time that the amount of aggregate Initial Development Costs incurred by the Parties first equals ********** Dollars ($**********).

1.185 "********** **Product**" means each product of AstraZeneca that is comprised of or contains **********, whether or not the **********, but excluding Combination Products.

1.186 "**Racemic Compound**" means Exo (1SR, 2SR, 4SR)-N,2,3,3-tetramethylbicyclo[2.2.1]heptan-2-amine**.**

1.187 "**Receiving Party**" has the meaning set forth in Section 8.2.2.

1.188 "**Regulatory Approval**" means, with respect to each Licensed Product and each country or jurisdiction, the granting or approval by the applicable Regulatory Authority of a Drug Approval Application for such Licensed Product in such country or jurisdiction.

1.189 "**Regulatory Authority**" means, as applicable, the FDA, EMEA, MHLW, PMDA or any other federal, state, local, national or supra-national agency, department, bureau or other government entity in any country in the Territory that holds responsibility for regulating the distribution, importation, exportation, Manufacture, use, storage, transport, Development, marketing or sale of a Licensed Product in such country, as used in any particular context hereunder, together with any successor thereto for the purpose contemplated in such context.

1.190 "**Regulatory Documentation**" means all applications, registrations, licenses, authorizations, approvals and correspondence submitted to or received from Regulatory Authorities (including minutes and official contact reports relating to any communications with any Regulatory Authority), and all supporting documents, relating to any Compound or Licensed Product, including all Drug Approval Applications, INDs and other Regulatory Filings, Adverse Event files and complaint files, but expressly excluding NDA ******** and IND ********.

1.191 "**Regulatory Filings**" means all communications, correspondence and documents submitted to a Regulatory Authority in connection with a Licensed Product, but excluding Drug Approval Applications. For clarity, Regulatory Filings are also Regulatory Documentation.

1.192 "**Regulatory/Pricing Approval**" means both (a) Regulatory Approval and (b) solely in the case of any country in which pricing or reimbursement approval is required, pricing or reimbursement approval.

1.193 "**Reverse Royalty Terminated Territory Product**" has the meaning set forth in Section 11.5.3(i).

1.194 "**Reverse Royalty Territory Product**" has the meaning set forth in Section 11.5.1(f).

1.195 "**ROW Territory**" means all of the countries and territories of the world other than the U.S. Territory.

1.196 "**Royalty Term**" means, with respect to each Licensed Product and each country in the Territory, the period beginning on the date of the first sale of such Licensed Product for use or consumption by the general public in such country after Regulatory Approval has been obtained in such country and ending on the later of:

(a) expiration of the last to expire Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Program Patent Rights, AstraZeneca Extended Term Patent Rights or Joint Program Patent Rights in such country that includes a Valid Claim that covers:

(i) the ******** of such Licensed Product;

(ii) a ******** or ******** such Licensed Product (including the ******** of such Licensed Product); or

(iii) a ******** of such Licensed Product for any ******** for which such Licensed Product has ******** (and, in the case of any country in which ******** or ******** is required, such ******** or ********) in such country, if, solely in the case of this clause (iii), no ******** (other than a ******** or ******** of ********) is ******** in such country a ******** that (A) is, if such country is the U.S. Territory, ******** in the ******** as a ******** that the ******** considers to be ******** such Licensed Product or (B) is, if such country is in the ROW Territory, ******** in the manner required by Applicable Laws in such country as ******** and ******** such Licensed Product; and

(b) twelve (12) years from the date of the First Commercial Sale of such Licensed Product in such country.

For clarity, with respect to any Licensed Product and country in the Territory, any Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Program Patent Rights, AstraZeneca Extended Term Patent Rights or Joint Program Patent Rights that are the subject of a patent term extension for such Licensed Product and country as contemplated by Section 7.9 shall not be deemed to have expired until expiration of such patent term extension.

1.197 "**Safety Agreement**" has the meaning set forth in Section 3.8.1.

1.198 "**Selling Party**" has the meaning set forth in the definition of "Net Sales."

1.199 "**sNDA**" means a Supplemental New Drug Application, as described in 21 C.F.R. §314.70, or any successor application in the U.S. Territory.

1.200 "******** **Notice**" has the meaning set forth in Section ********.

1.201 "**Sublicensee**" means a Third Party to which AstraZeneca or Targacept, as applicable, has granted a sublicense or license under any Patent Rights, Information or Inventions licensed to such Party pursuant to this Agreement.

1.202 "**Surviving Party**" has the meaning set forth in Section 6.1.2(b).

1.203 "**Targacept**" has the meaning set forth in the preamble hereto.

1.204 "**Targacept Additional Development Cost Notice**" has the meaning set forth in Section 3.9.1(c)(iv).

1.205 "**Targacept Additional Development Cost Threshold**" means, with respect to an Additional Development Project, (a) the amount designated by Targacept for such Additional Development Project in accordance with Section 3.9.1(c)(ii) (which amount, for clarity, may be $**********) or (b) if Targacept initially designates an amount greater than $********** for such Additional Development Project, such higher amount as may become applicable pursuant to, and determined in accordance with, Section 3.9.1(c)(iv).

1.206 "**Targacept Additional Development Cost Threshold Establishment Date**" has the meaning set forth in Section 3.9.1(c)(ii).

1.207 "**Targacept Change of Control Notice**" has the meaning set forth in Section 12.5.1.

1.208 "**Targacept Development Activities**" means the Development activities for one or more Compounds or Licensed Products (a) specified to be conducted by Targacept in the first Amplixa Annual Global Development Plan as agreed upon by the Parties as of the Execution Date, (b) specified after the Execution Date to be conducted by Targacept in any Amplixa Annual Global Development Plan, without resort to ********** (if applicable) pursuant to Section 2.1.5(a), or (c) that the Parties agree in writing shall be conducted by Targacept.

1.209 "**Targacept Indemnitees**" has the meaning set forth in Section 10.2.

1.210 "**Targacept Initial Development Cost Notice**" has the meaning set forth in Section 3.9.1(b)(ii).

1.211 "**Targacept Initial Development Cost Threshold**" means (a) ********** Dollars (US $**********) or (b) such higher amount as may become applicable pursuant to, and determined in accordance with, Section 3.9.1(b).

1.212 "**Targacept Know-How**" means, subject to Section 11.5.3(d)(i), any Information or Invention owned or Controlled by Targacept or any of its Affiliates on the Execution Date, during the period from the Execution Date until the Effective Date, or during the Term (including, for clarity, as between the Parties, Information discovered, developed or otherwise made during the Term in the conduct of Targacept Development Activities solely by one or more employees of or consultants to Targacept or any of its Affiliates) that is not generally known and that is necessary or reasonably useful for AstraZeneca to exercise any Development or Commercialization rights or perform any Development or Commercialization obligations hereunder, but excluding (a) Product Information, (b) Product Invention-Related Information, (c) Joint Program Information, (d) Program Inventions and (e) Inventions claimed or covered by Targacept Patent Rights, Targacept Program Patent Rights or Joint Program Patent Rights.

1.213 “**Targacept Licensed Product Information**” has the meaning set forth in Section 8.1.

1.214 “**Targacept Patent Rights**” means, subject to Section 7.7.1(c), all Patent Rights in the entire world owned or Controlled by Targacept or any of its Affiliates as of the Execution Date, during the period from the Execution Date until the Effective Date, or during the Term that claim the composition of matter, a method of Manufacture or use of or a pharmaceutical preparation containing or comprising (including the pharmaceutical composition of), or cover the research, development, Manufacture, use, import, offer to sell or sale of, any Compound or Licensed Product, including the Existing Patent Rights, but excluding Targacept Program Patent Rights and Joint Program Patent Rights.

1.215 “**Targacept Program Invention**” means each: (a) Program Invention for which one or more employees of or consultants to Targacept or any of its Affiliates are the sole inventors; and (b) Product Invention. Inventorship for purposes of this definition shall be determined by reference to United States patent laws in effect on the Execution Date irrespective of where such Invention is actually invented.

1.216 “**Targacept Program Patent Rights**” means all Patent Rights in the entire world that contain one or more claims that cover any Targacept Program Invention.

1.217 “**Targacept Sublicense Agreements**” means the USFRF Agreement and the Yale Agreement.

1.218 “**Targacept Technology**” means, collectively: (a) Targacept Patent Rights; (b) Targacept Know-How; (c) Targacept Program Inventions; (d) Product Invention-Related Information; (e) Targacept Program Patent Rights; and (f) Targacept’s interest in Joint Program Information, Joint Program Inventions and Joint Program Patent Rights.

1.219 “**Target Indication**” means the treatment, prevention, cure or delayed progression of MDD in humans.

1.220 “**Term**” has the meaning set forth in Section 11.1.

1.221 "**Terminated Territory**" means each Major Country with respect to which this Agreement is terminated by Targacept pursuant to Section 11.2.2 or by AstraZeneca pursuant to Section 11.3.2.

1.222 "**Territory**" means all of the countries and territories of the world, excluding each Terminated Territory, if any.

1.223 "**Third Party**" means any entity other than Targacept, AstraZeneca or an Affiliate of Targacept or AstraZeneca.

1.224 "**Trademark**" means any word, name, symbol, color, designation or device or any combination thereof for use in the course of trade, including any domain name, trademark, trade dress, brand mark, trade name, brand name, logo or business symbol, any registrations thereof or any pending applications thereto.

1.225 "**Unresolved Matter**" has the meaning set forth in Section 2.1.5(a).

1.226 "**Unshared Development Costs**" means, with respect to any Licensed Product, Development Costs that are specifically in furtherance of obtaining or maintaining Marketing Approval of such Licensed Product for any Indication in any country that is outside both the U.S. Territory and the EU but not also required to obtain or maintain Regulatory/Pricing Approval in the U.S. Territory or in any country in the EU (e.g., toxicology studies or Clinical Studies required to obtain or maintain Marketing Approval under Applicable Laws in Japan).

1.227 "**U.S. Territory**" means the United States of America and its territories and possessions, including Puerto Rico and the U.S. Virgin Islands.

1.228 "**USF/USFRF Agreement**" means, together, the Exclusive License Agreement, effective as of July 9, 1997, and the Exclusive License Agreement, effective as of October 10, 1998, in each case by and between USF and USFRF. "**USF**" means the University of South Florida and "**USFRF**" means the University of South Florida Research Foundation, Inc.

1.229 "**USFRF Agreement**" means the Amended and Restated License Agreement, dated as of March 9, 2004, by and between Targacept and USFRF, as amended and as may be further amended.

1.230 "**Valid Claim**" means a claim within: (a) an issued patent that has not (i) expired, lapsed or been finally cancelled or abandoned, (ii) been held unenforceable or invalid, or permanently revoked by a court or administrative or governmental agency of competent jurisdiction in an order or decision that is unappealable or unappealed within the time allowed for appeal or (iii) been abandoned, disclaimed, denied or admitted to be unenforceable through reissue, reexamination, disclaimer or otherwise; or (b) a pending patent application that was filed and is being prosecuted in good faith and has not been abandoned or finally disallowed without the possibility of appeal or re-filing of the application; provided that such application has not ******** for ******** its ********.

1.231 "**Voting Securities**" has the meaning set forth in Section 6.1.3(a)(i).

1.232 "**Voting Stock**" has the meaning set forth in the definition of "Change of Control."

1.233 "**Working Group**" has the meaning set forth in Section 2.2.

1.234 "**Yale Agreement**" means the Exclusive License Agreement, dated January 22, 2007, by and between Targacept and Yale, as may be amended. "**Yale**" means Yale University.

ARTICLE 2
GOVERNANCE OF THE COLLABORATION

2.1 **The Joint Development Committee**. Promptly and in any event within ******** days after the Effective Date, the Parties shall establish and convene a committee (the "**Joint Development Committee**" or "**JDC**") to oversee the Development Program as more specifically provided herein.

2.1.1 *Membership*. The JDC shall be comprised of ******** representatives (or such other number of representatives as the Parties may agree) of each of AstraZeneca and Targacept. Each Party shall provide the other Party with a list of its initial members of the JDC within ******** Business Days after the Effective Date. Each Party may replace any or all of its representatives on the JDC at any time upon written notice to the other Party in accordance with Section 12.2. Each representative of each Party shall be an employee of such Party at the level of ******** or ******** and shall have expertise in clinical development, pharmaceutical commercialization or regulatory affairs. Any member of the JDC may designate a substitute to attend and perform the functions of that member at any meeting of the JDC. Each Party may, in its reasonable discretion, invite non-member employees of such Party to attend meetings of the JDC as a non-voting participant, subject to the confidentiality obligations of Article 8. ******** representative shall be the chairperson of the JDC (the "**Chairperson**") to oversee the operation of the JDC and prepare minutes as set forth in Section 2.1.3.

2.1.2 *Meetings*.

(a) Until the termination or expiration of the Development Program, the JDC shall meet in person or otherwise at least once every ******** months, and more frequently as the Parties deem appropriate, on such dates as the Parties shall agree. The location of meetings of the JDC that are held in person shall alternate between the respective offices of the Parties or be held at such other place as the Parties may agree, with the first JDC meeting being held at Targacept's offices. The members of the JDC also may be polled or consulted from time to time by means of telecommunications, video conferences, electronic mail or correspondence, as deemed necessary or appropriate. Each Party shall be solely responsible for the expenses of its representatives to attend or participate in JDC meetings.

(b) Without limitation of Section 2.1.2(a), if any member of the JDC deems it appropriate to convene an additional JDC meeting in advance of the next regularly scheduled meeting: (i) such member shall contact each other member of the JDC in a manner appropriate under the circumstances; and (ii) AstraZeneca and Targacept shall cause their respective representatives on the JDC to use diligent efforts to identify a mutually acceptable date and time for such meeting to occur by telecommunications or video conference as soon as practicable thereafter, with a good faith target of within ******** Business Days after the first contact by the initiating JDC member to the first representative of the other Party on the JDC.

2.1.3 *Minutes*. The Chairperson shall have responsibility for preparing and circulating minutes within ******** Business Days after each meeting setting forth, *inter alia*, a description, in reasonable detail, of the discussions at the meeting and a list of any actions, decisions or determinations approved and a list of any issues to be resolved by the Executive Officers pursuant to Section 2.1.5(a). With the sole exception of specific items of the meeting minutes to which the members cannot agree and that are escalated to the Executive Officers as provided in Section 2.1.5(a), the JDC shall use diligent efforts to ensure that definitive minutes of all JDC meetings are finalized within ******** Business Days after the applicable meeting. If at any time during the preparation and finalization of the JDC minutes, the Parties do not agree on any issue with respect to the minutes, such issue shall be resolved by the escalation process as provided in Section 2.1.5(a), subject to Section 2.1.5(b). The decision of the JDC or, if applicable, any decision made as provided in Section 2.1.5(a) shall be recorded by the Chairperson in amended minutes for such meeting.

2.1.4 *Responsibilities of the JDC*. The JDC shall be responsible for overseeing the Development Program. Without limiting the generality of the foregoing, the JDC shall have the following responsibilities:

(a) direct the preparation of, and review and approve: (i) each Amplixa Annual Global Development Plan; provided that the Parties have agreed to the first Amplixa Annual Global Development Plan, which covers the period from the Effective Date through December 31, 2010, as of the Execution Date; (ii) any update or amendment to any Amplixa Annual Global Development Plan or the Amplixa Global Development Outline, subject to Section 3.1.1; and (iii) protocols (including subject population, inclusion/exclusion criteria, primary and secondary endpoints, dose selection, dosing regimen, duration of dosing, control and study design), success criteria, statistical analysis methodology and other material elements for each Clinical Study of a Licensed Product, to the extent not included in any previously approved Amplixa Annual Global Development Plan;

(b) monitor the execution of the Parties against each Amplixa Annual Global Development Plan, including the applicable budgets;

(c) review data, reports or other information submitted to it from time to time by either Party or any Working Group;

(d) oversee the performance of each Working Group;

(e) resolve all matters for which there is not consensus between one Party's representatives on a Working Group and the other Party's representatives on such Working Group;

(f) consider and determine the regulatory strategy for Development of Compounds and Licensed Products;

(g) determine whether a Milestone Event has occurred;

(h) serve as a vehicle to facilitate the transfer of information between the Parties with respect to all Development activities; and

(i) perform such other responsibilities as may be mutually agreed upon by the Parties from time to time; provided that, for clarity, the JDC shall not have the power to amend or modify this Agreement.

For clarity, no matter for which consent, approval or agreement of a Party is expressly required by any provision of this Agreement shall be within the responsibility of the JDC.

2.1.5 *Decision-making*.

(a) General. Except to the extent otherwise expressly provided herein, decisions of the JDC shall be made by consensus, with all representatives of each Party, collectively, having one (1) vote in all decisions. In the event that the JDC is unable to reach a consensus decision within ******** Business Days after it has met and attempted to reach such decision, either Party may, by written notice to the other Party, have such matter referred to ******** Targacept and ******** AstraZeneca and its Affiliates, or such other person holding a similar position designated by AstraZeneca from time to time (collectively, the "**Executive Officers**"), for resolution. The Executive Officers shall meet promptly to discuss the matter submitted and to determine a resolution. If the Executive Officers are unable to determine a resolution within ******** Business Days after the matter was first referred to them (each such matter, an "**Unresolved Matter**"), then the ******** shall ******** with regard to such Unresolved Matter, except that (a) the ******** shall not have such right with regard to the Unresolved Matters set forth in Section 2.1.5(b) (each an "**Excepted Decision**") and (b) in no event shall ******** (or, for clarity, the ********) have the right to assign ******** responsibility for, and unless ******** shall otherwise expressly consent, ******** shall have no responsibility for, performing any aspect of any ******** or performing any aspect of any Initial Development Activities other than those specified to be performed by ******** in the first Amplixa Annual Global Development Plan as agreed upon by the Parties as of the Execution Date. For clarity, neither any patent or other intellectual property matter nor any other matter not expressly specified as a JDC responsibility in Section 2.1.4 is (A) within the responsibilities of the JDC, (B) subject to the dispute escalation process of this Section 2.1.5(a) or (C) subject ******** of the ******** pursuant to this Section 2.1.5(a) (but, for clarity, such matter may be subject ******** of ******** to the extent expressly provided elsewhere in this Agreement).

(b) Excepted Decisions. Each of the following Unresolved Matters shall be an Excepted Decision:

(i) any matter with respect to an ******** or ********, including (A) whether to conduct a particular ********, (B) the identification of ******** to be conducted with respect to a particular ********, (C) the design, scope or conduct of any particular ******** and (D) with respect to each ******** (but except as provided in Section ********), the determination of the ******** required to trigger ******** right pursuant to Section ******** with respect to such ******** (such ********, the "*********");

(ii) any proposed ******** or amendment, modification or update thereto, or any proposed amendment, modification or update to the ********, that includes or impacts any of the matters covered by clause (i) above;

(iii) a determination as to whether any Milestone Event has occurred;

(iv) a disagreement as to whether a particular matter or decision is an Excepted Decision;

(v) any unresolved issue relating to a proposed ********; and

(vi) the content of the minutes of any JDC meeting with respect to any matter specified in the foregoing clauses (i) through (v).

The Parties shall work diligently and in good faith to resolve each Excepted Decision by consensus. For clarity: (A) neither Party (nor either Party's Executive Officer) shall have final decision-making authority with respect to an Excepted Decision; (B) notwithstanding anything in this Agreement to the contrary, ******** shall not have the right to conduct any Development activities to the extent that such activities would be inconsistent with any unresolved Excepted Decision; (C) no matter shall be an Excepted Decision to the extent such matter relates to ********; (D) all Development activities with respect to one or more ******** (regardless of the Development Costs with respect thereto) shall constitute ******** for the purposes of Section 2.1.5 (i.e., no matter with respect to such ******** activities shall be an Excepted Decision); and (E) no Excepted Decision, other than a determination as to whether any Milestone Event has occurred or as to whether a particular matter or decision is an Excepted Decision, shall be subject to dispute resolution pursuant to Section 12.1.

2.2 **Working Groups**. From time to time, the JDC may establish one or more subcommittees or working groups to oversee particular activities (each, a "**Working Group**"). In any event, the JDC shall establish a joint Working Group to oversee the operation of Co-Development Activities (the "**Development Working Group**"). Each Working Group shall consist of such number of members as the JDC determines is appropriate from time to time; provided that (a) unless the Parties agree otherwise, each Party shall have the same number of representatives on each Working Group and (b) each Party's Development Liaison shall be a member of the Development Working Group. Either Party's representatives on a Working Group at any time may escalate to the JDC for resolution any matter with respect to which such Party's representatives are not satisfied.

2.3 **Alliance Managers; Development Liaisons**.

2.3.1 Promptly after the Effective Date, each Party shall appoint an individual (other than an existing member of the JDC) to act as the project leader for such Party (each, an "**Alliance Manager**"). Each Alliance Manager shall thereafter be permitted to attend meetings of any Working Group and to attend meetings of the JDC (as a non-voting observer), subject to the confidentiality provisions of Article 8. The Alliance Managers shall be the primary point of contact for the Parties regarding the Collaboration (excluding matters that relate solely to Development or Commercialization). The Alliance Managers shall also be responsible for assisting the JDC in performing its oversight responsibilities. Each Party shall provide the other Party with the name and contact information for its Alliance Manager within ************ Business Days after the Effective Date. Each Party may replace its Alliance Manager at any time upon written notice to the other Party in accordance with Section 12.2.

2.3.2 Promptly after the Effective Date, each Party shall appoint an individual (other than an existing member of the JDC) to act as the Development liaison for such Party (each, a "**Development Liaison**"). Each Development Liaison shall thereafter be permitted to attend meetings of the JDC (as a non-voting observer), subject to the confidentiality provisions of Article 8. The Development Liaisons shall be the primary point of contact for the Parties regarding the Development Program and shall meet at least once a month to review and discuss the progress of the Development Program and any aspects thereof that either of them shall deem relevant. Such meetings shall be by telecommunication or video conference. Neither Party shall be obligated to prepare any printed materials in connection with such meetings, but each Party shall nevertheless use diligent efforts to provide such printed materials as may be reasonable under the circumstances to achieve the objective of each such meeting. The Development Liaisons shall also be responsible for assisting the JDC in performing its oversight responsibilities. Each Party shall provide the other Party with the name and contact information for its Development Liaison within ************ Business Days after the Effective Date. Each Party may replace its Development Liaison at any time upon written notice to the other Party in accordance with Section 12.2.

2.4 **Appointment of JDC Members, Alliance Managers and Development Liaisons**.

2.4.1 *Appointment is a Right.* The appointment of members of the JDC and an Alliance Manager and Development Liaison is a negotiated right of Targacept, waivable at any time, is not an obligation and shall not be a "deliverable" as referred to in Subtopic 25, "*Multiple-Element Arrangements*" of Accounting Standards Codification Topic 605, "*Revenue Recognition*." For clarity, Targacept shall be free to determine not to appoint members to the JDC (or to appoint fewer than the total number of members that it is eligible to appoint) and to determine not to appoint an Alliance Manager or a Development Liaison.

2.4.2 *Consequence of Non-Appointment.* If Targacept does not appoint members of the JDC, or does not appoint the total number of members that it is eligible to appoint, or does not appoint an Alliance Manager or a Development Liaison, it shall not be a breach of this Agreement, nor shall any consideration be required to be returned to AstraZeneca; provided that, with respect to the JDC, AstraZeneca shall have the votes and decision-making power of Targacept unless and until Targacept appoints at least one member of the JDC.

ARTICLE 3
DEVELOPMENT AND COMMERCIALIZATION OF LICENSED PRODUCTS; BACKUP R&D PROGRAMS

3.1 **Implementation of Development Programs**.

3.1.1 *Amplixa Global Development Outline and Amplixa Annual Global Development Plans*. The first Amplixa Annual Global Development Plan, which covers the period from the Effective Date through December 31, 2010, and the Amplixa Global Development Outline have been agreed upon by the Parties as of the Execution Date. For Calendar Year 2011 and for each Calendar Year thereafter during the Term, an Amplixa Annual Global Development Plan shall be prepared at the direction of the JDC and submitted to the JDC for approval; provided that the Parties shall manage the preparation of each such Amplixa Annual Global Development Plan in a manner designed to submit it for such JDC approval at least ******** Business Days before the meeting at which it will be considered and to obtain such JDC approval no later than ******** days prior to the end of the current Calendar Year. Each Amplixa Annual Global Development Plan shall, subject to Sections 2.1.5(a) and 2.1.5(b): (a) set forth for the applicable Calendar Year (i) the Development objectives, each Indication in the Field for which Development is to be conducted (which, for clarity, will constitute ******** if not the ********), Clinical Studies and other Development activities, priorities, timelines, budget and resources with reasonable specificity, (ii) whether activities are Targacept Development Activities or AstraZeneca Development Activities, (iii) with respect to such Co-Development Activities, the estimated number of FTEs to be allocated to perform such activities and the corresponding FTE Costs and (iv) a projection, based on available information, of those Co-Development Activities for which Development Costs will be Unshared Development Costs; and (b) be consistent with the terms of this Agreement and, unless the JDC shall otherwise determine, the Amplixa Global Development Outline then in effect; provided that if the JDC shall have determined, as expressly reflected in minutes of a JDC meeting and subject to Section 2.1.5(b), that an Amplixa Annual Global Development Plan need not be consistent with the Amplixa Global Development Outline on a particular matter, the Amplixa Global Development Outline need not be formally amended and shall be superseded in relevant part by such Amplixa Annual Global Development Plan. Each amendment, modification or update to any Amplixa Annual Global Development Plan or the Amplixa Global Development Outline shall: (x) except as set forth in the immediately preceding sentence, be set forth in a written document that specifically states that it is an amendment, modification or update to such Amplixa Annual Global Development Plan or the Amplixa Global Development Outline, as applicable, and be subject to approval by the JDC, and (y) include the resulting changes to the budget, if any.

3.1.2 *Responsibility for Development of Licensed Products.* Development of any Compound or Licensed Product shall be conducted in accordance with the Amplixa Annual Global Development Plans. With respect to each Compound or Licensed Product, unless otherwise set forth in any Amplixa Annual Global Development Plan approved by the JDC or agreed by the Parties in a writing that expressly references this Section 3.1.2: (a) with respect to Targacept Development Activities, Targacept shall have operational, day-to-day responsibility over the implementation of such activity (i.e., “how” it gets performed), but shall not have any strategic control over such activity (i.e., “whether” or “to what extent” it gets performed); (b) with respect to AstraZeneca Development Activities, AstraZeneca shall have operational, day-to-day responsibility over the implementation of such activity (i.e., “how” it gets performed), but, subject to Section 2.1.5, shall not have any strategic control over such activity (i.e., “whether” or “to what extent” it gets performed); and (c) AstraZeneca shall be solely responsible for all aspects of Manufacturing Development, subject to Section 3.3.

3.1.3 *Assignment of Regulatory Documentation*. Targacept hereby assigns to AstraZeneca all of its right, title and interest in and to all Regulatory Documentation and Product Regulatory Approvals (including the Amplixa IND) owned by Targacept as of the Execution Date and during the period from the Execution Date until the Effective Date. Targacept shall duly execute and deliver, or cause to be duly executed and delivered, such assignments, agreements, documents and instruments as both (a) may be necessary to carry out, or as AstraZeneca may reasonably request in connection with, this Section 3.1.3 and (b) shall be provided by AstraZeneca in reasonable and customary form, such execution and delivery by Targacept to be completed, with respect to each such assignment, agreement, document or instrument, not later than ******** Business Days after the later of (i) the Effective Date or (ii) the date of receipt thereof by Targacept.

3.1.4 *Information Disclosure; Assistance.* In connection with the transition of certain Development and regulatory activities from Targacept to AstraZeneca, Targacept shall, and shall cause its Affiliates to:

(a) disclose and make available to AstraZeneca within ******** after the Effective Date (unless previously provided): (i) the meeting request for an End of Phase 2 Meeting, (ii) the briefing package for an End of Phase 2 Meeting (in its then-current form) and all supporting documentation with respect thereto; and (iii) any written communications, and shall describe any oral communications, with the FDA related to an End of Phase 2 Meeting, in each case if any;

(b) disclose and make available to AstraZeneca within ******** Business Days after the Effective Date (unless previously provided): IND ********;

(c) disclose and make available to AstraZeneca within ******** days after the Effective Date (unless previously provided): all raw and final data sets and supporting data dictionaries, analyses and analytic results, and all clinical study reports and case report forms, in each case with respect to the Primary Compound;

(d) disclose and make available to AstraZeneca within ******** days after the Effective Date (unless previously provided): IND ********, IND ********, IND ********, IND ******** and NDA ********;

(e) use diligent efforts to disclose and make available to AstraZeneca as soon as reasonably practicable, and in any event within ******** days after the Effective Date, (unless previously provided): (i) the Regulatory Documentation; and (ii) all other Information owned or Controlled by Targacept that is related to Compounds or Licensed Products, including ******** and ********, and ********, with all ******** and ******** and ********, and ******** materials, and all ******** and ******** with ******** on issues relating specifically to the ******** of Compounds or Licensed Products for all Indications, in whatever form such Information exists in the possession of Targacept or its Affiliates on the Effective Date; and

(f) provide AstraZeneca with reasonable assistance required in order to transfer the Targacept Know-How to AstraZeneca in a timely manner. Without limiting the generality of this clause (f), if visits of Targacept's representatives to AstraZeneca's facilities are reasonably requested by AstraZeneca for purposes of transferring the Targacept Know-How to AstraZeneca or for purposes of AstraZeneca acquiring expertise on the practical application of the Targacept Know-How or assisting on issues arising during such Development or Commercialization, Targacept shall send appropriate representatives to AstraZeneca's facilities at a mutually acceptable time and frequency; provided that AstraZeneca shall reimburse Targacept for its reasonable and verifiable FTE Costs and direct out-of-pocket expenses related to such visits.

3.1.5 *Limitations on Development by Targacept.* Except as otherwise agreed by the Parties in writing, Targacept shall not, and shall cause it Affiliates not to, directly or through any Third Party, Develop any Compound or Licensed Product for use in the Field in the Territory, except for the Targacept Development Activities; provided that, for purposes of this Section 3.1.5, Targacept Development Activities include all actions taken by Targacept that it reasonably and in good faith believes are permitted by this Agreement and Targacept's performance of Section 3.3.4.

3.2 **Licensed Product Commercialization**.

3.2.1 *Right to Commercialize*. Subject to Targacept's rights and obligations under the Co-Promotion Agreement, if any, and subject to Sections 3.2.2, 3.2.3, 3.3 and 3.7.2, AstraZeneca shall have the sole and exclusive right to Commercialize Compounds and Licensed Products in the Field in the Territory.

3.2.2 *Executive Meetings*. The ******** for AstraZeneca's ******** and the ******** of Targacept (or, in each case, a substitute acceptable to the non-substituting Party, acting reasonably) shall meet at least ******** each Calendar Quarter in person at the offices of ******** to review and discuss such aspects of the historical or planned Commercialization of Licensed Products in the Territory as either of them shall deem relevant. Each Party shall be solely responsible for the expenses of its representative to attend or participate in such meetings.

3.2.3******** *Personnel*. AstraZeneca and Targacept shall work diligently and in good faith through the ******** for AstraZeneca's ******** and the ******** of Targacept to determine within ******** days after the Effective Date the ******** and, ********, terms of an arrangement whereby ******** employees with experience or expertise in one or more of ******** and ******** would participate with and contribute to initially, the ******** (or other similar) ******** for ********, and then the ******** (or other similar) ******** for ********, for the ******** Licensed Product; provided that if after such ******** period, the Parties have not agreed upon whether such arrangement would be ******** or, ********, the terms of such arrangement, the matter shall be referred to the ******** of Targacept and the ******** of AstraZeneca's ******** for resolution. If despite good faith negotiations such officers cannot resolve such matter within ******** Business Days after it has been referred to them, then neither Party shall ******** with respect thereto. ******** such an arrangement is established, approximately ******** days prior to the projected date on which the ******** (or other similar) ******** for ******** would first become active in ******** activities for the first Licensed Product, the Parties would consider in good faith any appropriate modifications to such arrangement. The Parties ******** that (a) such ******** employees would be ******** at ******** of ******** and (b) ******** would be responsible for all ******** and ******** related to such employees.

3.3 **Manufacturing**.

3.3.1 *Manufacturing of Licensed Products*. Without limitation of Section 3.2, subject to Sections 3.3.2 and 3.3.4, AstraZeneca shall have the sole and exclusive right to (a) conduct or have conducted Manufacturing Development with respect to Compounds and Licensed Products and (b) Manufacture or have Manufactured Compounds and Licensed Products. For clarity, subject to the terms of the Existing TRGT API Agreements with respect to the Primary Compound, AstraZeneca shall have the right, in its sole discretion, to determine the specifications with respect to any Compound or Licensed Product.

3.3.2 *Existing TRGT API Agreements and* ******** *Agreement*. As soon as practicable after the Effective Date, Targacept shall assign (a) its Amended and Restated Supply Agreement dated December 3, 2009 by and among Targacept, Poli Industria Chimica, SpA and Interchem Corporation (the "**Existing TRGT Supply Agreement**") and the related Quality Agreement dated December 3, 2009 by and among Targacept, Poli Industria Chimica, SpA and Interchem Corporation (together with the Existing TRGT Supply Agreement, the "**Existing TRGT API Agreements**") and (b) its Master Service Agreement between Targacept and ******** dated August 13, 2009, and Work Order No. 1, dated August 13, 2009, thereunder (collectively, the "******** **Agreement**"), in each case (clauses (a) and (b)) to AstraZeneca, and AstraZeneca shall accept such assignment and assume all of Targacept's rights and obligations under the Existing TRGT API Agreements and the ******** Agreement pursuant to an assignment and assumption agreement substantially in the form of Schedule 5 attached hereto. Each Party shall duly and punctually perform all of its obligations under such assignment and assumption agreement.

3.3.3 *Assignment of Primary Compound and Primary Compound Licensed Products*. Targacept hereby assigns to AstraZeneca all of its right, title and interest in and to any and all supply of the Primary Compound and Primary Compound Licensed Product owned by Targacept and existing as of the Effective Date, wherever located, including finished tablets and work in process, for ********.

3.3.4 *Cooperation Regarding Capsules.* At AstraZeneca's request, Targacept shall cooperate in all reasonable respects to secure supply of Licensed Products in capsule form for the conduct of the Development Program from ******** pursuant to Targacept's current master services agreement with ********.

3.4 **Diligence**.

3.4.1 *Development and Commercialization*. During the Term, (a) with respect to each Licensed Product, AstraZeneca shall, without limitation of clause (b) below, use Commercially Reasonable Efforts to conduct the AstraZeneca Development Activities and Targacept shall use Commercially Reasonable Efforts to conduct the Targacept Development Activities and (b) AstraZeneca shall use Commercially Reasonable Efforts to Develop, obtain Marketing Approval (including, for clarity, Regulatory/Pricing Approval) for, launch and otherwise Commercialize ******** Licensed Product for ******** Indication in each Major Country. Notwithstanding anything herein to the contrary, to the extent that AstraZeneca would be required to perform ******** to satisfy its obligations under the first sentence of this Section 3.4.1 and Targacept's representatives on the JDC withhold their consent to such ********, then AstraZeneca's failure to perform such ******** shall not constitute a breach of AstraZeneca's obligations under this Section 3.4.1. Except as set forth in this Section 3.4.1 or, with respect to Targacept, the Co-Promotion Agreement, if any, neither Party shall have any diligence obligations with respect to the Development or Commercialization of Compounds or Licensed Products. Targacept acknowledges that (x) AstraZeneca and its Affiliates have ******** for the commercialization of their products, (y) AstraZeneca and its Affiliates intend to continue research, development and commercialization of one or more ******** during the Term and shall have the right to continue to do so in the ordinary course of business and (z) in the ordinary course of business, AstraZeneca and its Affiliates ******** of their products, including ******** and Licensed Products.

3.4.2 ******** *Development* ******** *Right.*

(a) Conditional Right. If at any time ******** a reasonable good faith belief that ******** is unwilling or unable to successfully perform one or more of the ******** Development Activities in accordance with the timeline for such ******** Development Activities contemplated by the applicable Amplixa Annual Global Development Plan, ******** shall have the right, at ********, to assume and complete some or all of such ******** Development Activities (the "******** **Development** ******** **Right**"); provided that: (i) in no event shall ******** have or be entitled to exercise the ******** Development ******** Right unless and until (A) ******** shall have ******** of the specific ******** Development Activities with respect to which ******** good faith belief applies (a "******** **Notice**") and (B) the Executive Officers (or, in the case of ********, a designee thereof) shall have met in person at a neutral location in Washington D.C. designated by ******** to discuss ******** good faith belief, and, at any time after such meeting ******** shall have confirmed to ******** that it continued to have such good faith belief; provided that, if the Executive Officer of ******** is not available for such meeting within ******** Business Days after delivery by ******** of the ******** Notice, then ******** may exercise the ******** Development ******** Right upon written notice to ******** given at any time after such ******** Business Day period regardless of whether such meeting has occurred; and (ii) the ******** Development ******** Right shall be subject to Section 3.4.2(b). If ******** so elects to exercise the ******** Development ******** Right with respect to any ******** Development Activities, to the extent requested by ******** in writing, ******** shall assign to ******** any or all Third Party agreements relating to such ******** Development Activities (including agreements with contract research organizations, clinical sites and investigators), unless, with respect to any such agreement, such agreement (A) expressly prohibits such assignment, in which case ******** shall cooperate with ******** in all reasonable respects to secure the consent of the applicable Third Party to such assignment, or (B) relates to activities in addition to such ******** Development Activities in which case, ******** would be required, at ******** sole cost and expense, to cooperate with ******** in all reasonable respects to facilitate the execution of a new agreement between ******** and the applicable Third Party with respect to such ******** Development Activities. If ******** assumes control of any such ******** Development Activities, then at ******** request and expense, ******** shall provide ******** with such reasonable assistance as is necessary to effectuate a smooth and orderly transition of such ******** Development Activities so as to minimize any disruption of such activities. With respect to all such ******** Development Activities that involve Clinical Studies for any Compound or Licensed Product, at ********'s option, ******** shall either (1) end such Clinical Studies with respect to enrolled subjects in an orderly and prompt manner in accordance with Applicable Laws, including any required follow up treatment with previously enrolled subjects, or (2) transfer control to ******** or its designee of such Clinical Studies and cooperate with ******** in all reasonable respects to ensure a smooth and orderly transition thereof that will not involve any disruption of such studies.

(b) ******** Right to Arbitrate. If ******** does not agree with ******** assertion that ******** is unwilling or unable to successfully perform one or more of the ******** Development Activities in accordance with the timeline for such ******** Development Activities contemplated by the applicable Amplixa Annual Global Development Plan and ******** nevertheless exercises the ******** Development ******** Right as provided in Section 3.4.2(a), ******** shall have the right, at its sole election, to submit such matter to arbitration pursuant to Section 12.1.2; provided that, for clarity, ******** shall have the right to proceed as provided in Section 3.4.2(a) notwithstanding such submission by ********. If it is determined in such arbitration proceeding that, at the time of ******** delivery of the ******** Notice, ******** was using Commercially Reasonable Efforts to conduct the ******** Development Activities in question, ******** shall be responsible for funding ******** percent (********%) of all Development Costs with respect to such activities incurred after ******** exercised its ******** Development ******** Right with respect thereto.

3.5 **Compliance**. Each Party shall perform its Development responsibilities and AstraZeneca shall perform its Commercialization responsibilities in good scientific or commercial manner, as the case may be, and in compliance in all material respects with all Applicable Laws. For clarity, with respect to each activity performed under an Amplixa Annual Global Development Plan that will or would reasonably be expected to be submitted to a Regulatory Authority in support of a Drug Approval Application, the Party performing such activity shall comply with, if and as applicable, the regulations and guidance of the FDA that constitute GLP, current Good Manufacturing Practices or Good Clinical Practices (or, if and as applicable under the circumstances, International Conference on Harmonization (ICH) guidance or other comparable regulation and guidance of any Regulatory Authority in the ROW Territory).

3.6 **Cooperation**. Scientists and other personnel at Targacept and AstraZeneca shall cooperate in all reasonable respects in the performance of their respective responsibilities hereunder and, subject to the terms of this Agreement and any confidentiality obligations to Third Parties, shall exchange such data, information and materials as is necessary or reasonably useful for the other Party to perform its obligations under any Amplixa Annual Global Development Plan.

3.7 **Exchange of Reports; Information; Updates**.

3.7.1 *Development Program Reports*.

(a) Targacept Development Activities. Targacept shall keep the JDC and AstraZeneca's Development Liaison regularly informed of the progress of its efforts with respect to the Targacept Development Activities. Without limiting the generality of the foregoing, Targacept shall, at each regular meeting of the JDC, provide the JDC and AstraZeneca's Development Liaison with a report in reasonable detail that summarizes the status of all Targacept Development Activities, together with such information that it has in its possession as may be reasonably requested from time to time by the JDC or AstraZeneca's Development Liaison.

(b) AstraZeneca Development Activities. AstraZeneca shall keep the JDC and Targacept's Development Liaison regularly informed of the progress of its efforts with respect to the AstraZeneca Development Activities. Without limiting the generality of the foregoing, AstraZeneca shall, at each regular meeting of the JDC, provide the JDC and Targacept's Development Liaison with a report in reasonable detail that summarizes the status of all AstraZeneca Development Activities, together with such information that it has in its possession as may be reasonably requested from time to time by the JDC or Targacept's Development Liaison.

(c) Information and Records. Each Party shall maintain, or cause to be maintained, such data, results and analyses, and all records of its Co-Development Activities under this Agreement, in sufficient detail and in good scientific manner appropriate for patent and regulatory purposes, which shall: (i) be complete and accurate in all material respects and reflect in all material respects all work done and results achieved in the performance of its activities hereunder; and (ii) be retained for at least ******** years after the Term or for such longer period as may be required by Applicable Laws. Each Party shall use diligent efforts to ensure that such records include only such activities and do not include and are not commingled with records of activities outside the Collaboration. Each Party shall have the right, during normal business hours and at a mutually convenient time, to inspect and copy any such records of the other Party. Each Party shall notify the other Party prior to destroying such records and the other Party shall have the right to take custody of such records within ******** Business Days after receipt of such notice.

3.7.2 *Commercialization Reports*. In addition to and not in limitation of Section 3.2.2 and 3.2.3, AstraZeneca shall provide Targacept:

(a)(i) at least ******** days, but not more than ******** days, prior to the projected submission date for the first NDA for the first Licensed Product, (A) the Amplixa ******** for AstraZeneca's U.S.-based Affiliate and (B) the Amplixa ******** for AstraZeneca's U.S.-based Affiliate, in each case (clauses (A) and (B)) as such document exists as of the time of delivery to Targacept (such documents collectively, the "**Amplixa Co-Promotion Information Documents**"), and (ii) each update, amendment or modification made to any Amplixa Co-Promotion Information Document, if any, promptly after such update, amendment or modification is made; and

(b) a written update summarizing in reasonable detail the plans for, and progress and results of, Commercialization activities for each Licensed Product in each of the Major Countries no less frequently than every ********.

In addition, at Targacept's reasonable request, AstraZeneca shall use diligent efforts to answer any questions Targacept has with respect to the Amplixa Co-Promotion Information Documents accurately and in a manner designed in good faith to provide Targacept sufficient time to take such answers into account in making its decision whether to exercise the Co-Promotion Right.

3.7.3 *Regulatory Matters.*

(a) Regulatory Filings and Drug Approval Applications. Subject to Sections 2.1.4 and 2.1.5(b) and this Section 3.7.3(a), with respect to each Compound or Licensed Product, AstraZeneca shall have the sole right to prepare and make all Drug Approval Applications and all Regulatory Filings (including reports of Adverse Events, if and to the extent required by Applicable Laws) in the Territory; provided that AstraZeneca shall (i) collaborate closely with Targacept throughout the preparation of each Development Regulatory Filing and consider all comments of Targacept with respect thereto in good faith, taking into account the best interests of the Development and Commercialization of the applicable Compound or Licensed Product on a global basis, and (ii) promptly provide Targacept with copies of each document or other correspondence received from a Regulatory Authority in a Major Country pertaining to the Development of such Compound or Licensed Product. Without limiting the generality of the foregoing proviso: (A) unless prohibited by any Third Party confidentiality obligations, AstraZeneca shall provide Targacept with each draft of each Development Regulatory Filing with respect to such Compound or Licensed Product, sufficiently in advance of its submission so that Targacept shall have an opportunity reasonable under the circumstances to review and comment on the substance of such Development Regulatory Filing (and, if prohibited by any Third Party confidentiality obligations, use diligent efforts to provide Targacept sufficient information with respect to such Development Regulatory Filing to enable Targacept to provide meaningful input with respect thereto); and (B) to the extent any such draft is other than in the English language, AstraZeneca shall cooperate with Targacept in all reasonable respects to cause such draft to be translated into English (at Targacept's reasonable expense) on a timely basis.

(b) FDA Meetings. With respect to each Licensed Product, AstraZeneca shall provide Targacept with at least ******** days written notice of any meeting with the FDA relating to the Development of such Licensed Product, except that, if AstraZeneca learns of the date scheduled by the FDA for such meeting fewer than ******** days before such scheduled date, AstraZeneca shall instead provide written notice of such meeting to Targacept within ******** Business Days after the date on which AstraZeneca learned of such scheduled date. With respect to each such meeting, Targacept shall have the right, but not the obligation, to send ******** (or such greater number, if any, as AstraZeneca may expressly agree) person to participate as ******** (at Targacept's sole cost and expense) in such meeting.

(c) Ownership. Subject to Section 11.5, all Drug Approval Applications, Product Regulatory Approvals and other Regulatory Documentation shall be the property of AstraZeneca and held in the name of AstraZeneca or its Affiliates.

3.8 **Safety Agreement; Adverse Event Reporting; Complaints; Product Recall**.

3.8.1 *Safety Agreement*. The rights and obligations of the Parties (and their Affiliates) with respect to safety and related reporting activities with respect to each Licensed Product shall be set forth in a safety agreement in a form mutually acceptable to the Parties (the "**Safety Agreement**"), which the Parties shall enter into no later than ******** Business Days after the Effective Date.

3.8.2 *Adverse Event Reporting*. Without limitation of Section 3.8.1, upon transfer of the Amplixa IND to AstraZeneca, AstraZeneca shall be responsible for Adverse Event reporting to applicable Regulatory Authorities in the Territory, shall comply with Applicable Laws with respect to Adverse Event reporting and shall maintain the global safety database for Licensed Products; except that Targacept shall be responsible for Adverse Event reporting to applicable Regulatory Authorities in the Territory as required with respect to NDA ******** and IND ********.

3.8.3 *Product Recall*.

(a) Notification and Recall. In the event that any Regulatory Authority issues or requests a recall or takes similar action in connection with any Compound or Licensed Product or, in the event AstraZeneca determines that an event, incident or circumstance has occurred that may result in the need for a recall or market withdrawal with respect to any Compound or Licensed Product, AstraZeneca shall promptly consult with at least one of Targacept's ******** (or ********) or ******** by telephone to discuss and consider such matter and AstraZeneca shall consider in good faith such Targacept representative's comments with respect thereto. Following such telephone call, AstraZeneca shall have final decision-making authority and control of whether to conduct such a recall or market withdrawal (except in the case of a government-mandated recall) in the Territory and the manner in which any such recall or market withdrawal shall be conducted.

(b) Recall Expenses. AstraZeneca shall bear all expenses of any recall or market withdrawal of any Compound or Licensed Product except to the extent such recall or market withdrawal resulted from any breach by Targacept of this Agreement or the Co-Promotion Agreement or from Targacept's or any of its Affiliates' negligence or willful misconduct, in which case Targacept shall bear the expenses of such recall or market withdrawal to the extent attributable to such breach, negligence or willful misconduct.

3.9 **Development Costs; Reconciliation and Auditing**.

3.9.1 *Responsibility for Development Costs.*

(a) Generally. Subject to Sections 3.4.2(b), 3.9.1(b) and 3.9.1(c), with respect to each Compound and Licensed Product, Targacept shall be responsible for funding its Co-Development Percentage of the total Development Costs for such Compound or Licensed Product and AstraZeneca shall be responsible for funding its Co-Development Percentage of the total Development Costs for such Compound or Licensed Product, except that, notwithstanding the foregoing, AstraZeneca shall be responsible for funding one hundred percent (100%) of all Unshared Development Costs for such Compound or Licensed Product, if any.

(b) Initial Development Costs.

(i) Notwithstanding anything to the contrary in this Agreement, in no event shall Targacept be required to fund cumulative Initial Development Costs in excess of the Targacept Initial Development Cost Threshold. Notwithstanding anything to the contrary in this Agreement, the Parties acknowledge and agree that aggregate Development Costs incurred by the Parties with respect to one or more ********, and no more, shall be deemed to be Initial Development Costs.

(ii) In the event that at any time during a Calendar Quarter Targacept has incurred cumulative Initial Development Costs that equal or exceed the Targacept Initial Development Cost Threshold then in effect, Targacept may, in its sole discretion and upon written notice to AstraZeneca (a "**Targacept Initial Development Cost Notice**"), elect to (A) increase the Targacept Initial Development Cost Threshold to the amount set forth in such Targacept Initial Development Cost Notice or (B) terminate its obligation to fund any Initial Development Costs in excess of the Targacept Initial Development Cost Threshold then in effect; provided that such Targacept Initial Development Cost Notice must be given no later than ************ Business Days after receipt by Targacept of the Development Cost Reconciliation Report for such Calendar Quarter showing that Targacept has incurred cumulative Initial Development Costs that equal or exceed the Targacept Initial Development Cost Threshold then in effect (an "**Initial Notice Deadline**").

(iii) If Targacept gives a Targacept Initial Development Cost Notice by the Initial Notice Deadline with respect to a particular Calendar Quarter and elects to:

(A) increase the Targacept Initial Development Cost Threshold, then the Targacept Initial Development Cost Threshold shall be increased to the amount set forth in such Targacept Initial Development Cost Notice; or

(B) terminate its obligation to fund any Initial Development Costs in excess of the Targacept Initial Development Cost Threshold then in effect, then (1) the Targacept Initial Development Cost Threshold shall no longer be subject to increase and shall be final and (2) AstraZeneca shall be solely responsible for funding ************ percent (************%) of all Initial Development Costs (regardless of which Party incurs such Initial Development Costs) in excess of such Targacept Initial Development Cost Threshold (including, for clarity, any such excess incurred prior to such Targacept Initial Development Cost Notice) and shall have the rights set forth in Section 5.11.1; provided that Targacept shall continue to have the responsibility to provide the reports contemplated by this Agreement, including Section 3.9.2(a), in each case to the extent applicable.

(iv) If Targacept does not give a Targacept Initial Development Cost Notice by the Initial Notice Deadline with respect to a particular Calendar Quarter:

(A) the Targacept Initial Development Cost Threshold shall automatically be increased to an amount equal to the cumulative Initial Development Costs incurred by Targacept as of the last day of the next Calendar Quarter (i.e., the Calendar Quarter in which such Initial Notice Deadline occurs); and

(B) for clarity, Targacept shall again have the right to give a Targacept Initial Development Cost Notice with respect to the next Calendar Quarter (i.e., the Calendar Quarter in which such Initial Notice Deadline occurs) by the Initial Notice Deadline for such next Calendar Quarter.

(v) For clarity, the amount of Initial Development Costs incurred by Targacept for the purpose of determining whether Targacept has incurred Initial Development Costs equal to, or in excess of, the Targacept Initial Development Cost Threshold then in effect shall be equal to the sum of the Initial Development Costs actually incurred by Targacept less any amounts received by Targacept from AstraZeneca pursuant to Section 3.9.2(a)(ii) (or, with respect to the most recently completed Calendar Quarter, that would be received by Targacept from AstraZeneca pursuant to Section 3.9.2(a)(ii) but for the application of this Section 3.9.1(b)) plus any amounts payable by Targacept to AstraZeneca pursuant to Section 3.9.2(a)(ii) (or, with respect to the most recently completed Calendar Quarter, that would be payable by Targacept to AstraZeneca pursuant to Section 3.9.2(a)(ii) but for the application of this Section 3.9.1(b)).

(c) Additional Development Costs; **********.

(i) Notwithstanding anything to the contrary in this Agreement, in no event shall Targacept be required to fund cumulative Additional Development Costs with respect to any Additional Development Project in excess of the Targacept Additional Development Cost Threshold for such Additional Development Project.

(ii) With respect to each Additional Development Project (but subject, with respect to **********, to clause (vi) below), prior to the earlier of (A) the date of commencement by Targacept of any Additional Development Activities with respect to such Additional Development Project and (B) the date that is ********** days after approval by the JDC of the Amplixa Annual Global Development Plan or update or amendment thereto providing for such Additional Development Project (such earlier date, the "**Targacept Additional Development Cost Threshold Establishment Date**"), Targacept shall notify AstraZeneca of the Targacept Additional Development Cost Threshold with respect to such Additional Development Project.

(iii) In the event that Targacept does not notify AstraZeneca of the Targacept Additional Development Cost Threshold with respect to any Additional Development Project prior to the Targacept Additional Development Cost Threshold Establishment Date for such Additional Development Project, the Targacept Additional Development Cost Threshold with respect to such Additional Development Project shall be $********, unless Targacept shall expressly agree otherwise in writing. If the Targacept Additional Development Cost Threshold with respect to any Additional Development Project is $********, AstraZeneca shall be solely responsible for funding ******** percent (********%) of all Additional Development Costs with respect to such Additional Development Project and AstraZeneca shall have the rights set forth in Section 5.11.2.

(iv) If the Targacept Additional Development Cost Threshold with respect to any Additional Development Project is greater than $********, in the event that at any time during a Calendar Quarter Targacept has incurred cumulative Additional Development Costs with respect to such Additional Development Project that equal or exceed the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect, Targacept may, in its sole discretion and upon written notice to AstraZeneca (a "**Targacept Additional Development Cost Notice**"), elect to (x) increase the Targacept Additional Development Cost Threshold with respect to such Additional Development Project to the amount set forth in such Targacept Additional Development Cost Notice or (y) terminate its obligation to fund any Additional Development Costs with respect to such Additional Development Project in excess of the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect; provided that such Targacept Additional Development Cost Notice with respect to such Additional Development Project must be given no later than ******** Business Days after receipt by Targacept of the Development Cost Reconciliation Report for such Calendar Quarter showing that Targacept has incurred cumulative Additional Development Costs with respect to such Additional Development Project that equal or exceed the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect (an "**Additional Notice Deadline**").

(A) If Targacept gives a Targacept Additional Development Cost Notice with respect to such Additional Development Project by the Additional Notice Deadline with respect to a particular Calendar Quarter and elects to:

(1) increase the Targacept Additional Development Cost Threshold with respect to such Additional Development Project, then the Targacept Additional Development Cost Threshold with respect to such Additional Development Project shall be increased to the amount set forth in such Targacept Additional Development Cost Notice; or

(2) terminate its obligation to fund any Additional Development Costs with respect to such Additional Development Project in excess of the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect, then (x) the Targacept Additional Development Cost Threshold with respect to such Additional Development Project shall no longer be subject to increase and shall be final and (y) AstraZeneca shall be solely responsible for funding ******** percent (********%) of all Additional Development Costs with respect to such Additional Development Project (regardless of which Party incurs such Additional Development Costs) in excess of such Targacept Additional Development Cost Threshold (including, for clarity, any such excess incurred prior to such Targacept Additional Development Cost Notice) and shall have the rights set forth in Section 5.11.2; provided that Targacept shall continue to have the responsibility to provide the reports contemplated by this Agreement, including Section 3.9.2(a), in each case to the extent applicable.

(B) If Targacept does not give a Targacept Additional Development Cost Notice with respect to such Additional Development Project by the Additional Notice Deadline with respect to a particular Calendar Quarter:

(1) the Targacept Additional Development Cost Threshold with respect to such Additional Development Project shall automatically be increased to an amount equal to the cumulative Additional Development Costs with respect to such Additional Development Project incurred by Targacept as of the last day of the next Calendar Quarter (i.e., the Calendar Quarter in which such Additional Notice Deadline occurs); and

(2) for clarity, Targacept shall have the right to give a Targacept Additional Development Cost Notice with respect to such Additional Development Project with respect to the next Calendar Quarter (i.e., the Calendar Quarter in which such Additional Notice Deadline occurs) by the Additional Notice Deadline for such next Calendar Quarter.

(v) For clarity, the amount of Additional Development Costs with respect to an Additional Development Project incurred by Targacept under Section 3.9.1(c)(iv) for the purpose of determining whether Targacept has incurred Additional Development Costs with respect to such Additional Development Project equal to, or in excess of, the Targacept Additional Development Cost Threshold for such Additional Development Project shall be equal to the sum of the Additional Development Costs for such Additional Development Project actually incurred by Targacept less any amounts received by Targacept from AstraZeneca pursuant to Section 3.9.2(a)(iii) with respect to such Additional Development Project (or, with respect to the most recently completed Calendar Quarter, that would be received by Targacept from AstraZeneca pursuant to Section 3.9.2(a)(iii) but for the application of this Section 3.9.1(c)) plus any amounts payable by Targacept to AstraZeneca pursuant to Section 3.9.2(a)(iii) with respect to such Additional Development Project (or, with respect to the most recently completed Calendar Quarter, that would be payable by Targacept to AstraZeneca pursuant to Section 3.9.2(a)(iii) but for the application of this Section 3.9.1(c)).

(vi) Notwithstanding anything to the contrary in this Agreement, the Parties acknowledge and agree that: (A) all Development Costs with respect to Development of one or more ******** in excess of the ******** shall be deemed to be Additional Development Costs; (B) all Development activities with respect to one or more ******** undertaken after all Development Costs with respect to ******** equal the ******** shall be deemed a single Additional Development Project solely for purposes of this Section 3.9.1(c) and Section 5.11.2, if applicable; (C) the Additional Development Cost Threshold with respect to such Additional Development Project shall be $********, unless Targacept shall expressly agree otherwise in writing; and (D) the ******** with respect to such Additional Development Project shall be the first receipt of Regulatory/Pricing Approval of a ******** for the ******** in a ********.

3.9.2 *Reconciliation of Development Costs.*

(a) Reports; Reconciliation of Development Costs. With respect to each Compound and Licensed Product, within ******** days following the end of each Calendar Quarter during the Term, each of Targacept and AstraZeneca shall submit to the JDC and to the other Party a written report setting forth in reasonable detail all Development Costs incurred by Targacept or AstraZeneca, as applicable, during such Calendar Quarter for such Compound or Licensed Product, broken out between Initial Development Costs and Additional Development Costs, if any, and by individual Additional Development Projects, and between Unshared Development Costs and all other Development Costs; provided that AstraZeneca shall have no obligation to report any Unshared Development Costs to Targacept. Upon the request of the Party receiving such report, the Party delivering such report shall provide copies of invoices or other appropriate supporting documentation for any payments made by such Party or any of its Affiliates to Third Parties that individually exceed ******** Dollars (US $********) or such other amount as may be determined by the Parties. Within ******** days following the receipt by the JDC of such written reports, the JDC shall prepare and submit to each Party a written report (each such report, a "**Development Cost Reconciliation Report**") setting forth in reasonable detail: (i) the calculation of all such Development Costs incurred by both Parties during such Calendar Quarter (and on a cumulative basis) for such Compound or Licensed Product, broken out between Initial Development Costs and Additional Development Costs, if any, and by individual Additional Development Projects, and between Unshared Development Costs (if any) and all other Development Costs; (ii) the calculation of the net amount owed by AstraZeneca to Targacept, or by Targacept to AstraZeneca, in order to ensure the funding of such Initial Development Costs (excluding, for clarity, Unshared Development Costs) in accordance with Section 3.9.1; provided that the JDC shall not be obligated to provide the calculation set forth in clause (ii) after Targacept elects to terminate its obligation to fund any Initial Development Costs in excess of the Targacept Initial Development Cost Threshold then in effect pursuant to Section 3.9.1(b)(ii); and (iii) the calculation of the net amount owed by AstraZeneca to Targacept, or by Targacept to AstraZeneca, in order to ensure the funding of such Additional Development Costs (excluding, for clarity, Unshared Development Costs) with respect to each Additional Development Project in accordance with Section 3.9.1; provided that the JDC shall not be obligated to provide the calculation set forth in clause (iii) for any Additional Development Project for which the Targacept Additional Development Cost Threshold is $******** or with respect to which Targacept elects to terminate its obligation to fund any Additional Development Costs in excess of the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect pursuant to Section 3.9.1(c)(iv), as the case may be. The net amounts payable pursuant to clauses (ii) and (iii) in the immediately preceding sentence shall be paid by Targacept or AstraZeneca, as applicable, to the other Party within ******** days after the distribution by the JDC of each Development Cost Reconciliation Report. For clarity: (A) if Targacept elects to terminate its obligation to fund any Initial Development Costs in excess of the Targacept Initial Development Cost Threshold then in effect pursuant to Section 3.9.1(b)(ii), the net amounts payable pursuant to clause (ii) above shall be determined so as to ensure that the maximum amount of Initial Development Costs funded by Targacept does not exceed such Targacept Initial Development Cost Threshold; (B) for each Additional Development Project with respect to which Targacept elects to terminate its obligation to fund any Additional Development Costs in excess of the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect pursuant to Section 3.9.1(c)(iv), if any, the net amounts payable pursuant to clause (iii) above shall be determined so as to ensure that the maximum amount of Additional Development Costs funded by Targacept with respect to such Additional Development Project does not exceed such Targacept Additional Development Cost Threshold for such Additional Development Project; (C) in the event Targacept has incurred Initial Development Costs in excess of the Initial Development Cost Threshold then in effect and this Agreement is terminated pursuant to Article 11 prior to the Initial Notice Deadline with respect to the Calendar Quarter in which such Initial Development Cost Threshold was so exceeded, Targacept shall be deemed to have given a Targacept Initial Development Cost Notice immediately prior to effectiveness of such termination electing to terminate its obligation to fund any Initial Development Costs in excess of the Targacept Initial Development Cost Threshold then in effect; and (D) in the event Targacept has incurred Additional Development Costs with respect to any Additional Development Project for which the Targacept Additional Development Cost Threshold is greater than $******** in excess of the Additional Development Cost Threshold then in effect for such Additional Development Project and this Agreement is terminated pursuant to Article 11 prior to the Additional Notice Deadline with respect to the Calendar Quarter in which such Additional Development Cost Threshold was so exceeded, Targacept shall be deemed to have given a Targacept Additional Development Cost Notice with respect to such Additional Development Project immediately prior to effectiveness of such termination electing to terminate its obligation to fund any Additional Development Costs with respect to such Additional Development Project in excess of the Targacept Additional Development Cost Threshold with respect to such Additional Development Project then in effect.

(b) Records; Development Cost Audit Rights. Each Party shall keep and maintain for ******** years complete and accurate records of Development Costs incurred with respect to each Compound or Licensed Product in sufficient detail to allow confirmation of same by the JDC and the other Party, including confirmation of the proper allocation of FTEs to Development of such Compound or Licensed Product. Each Party (the "**Cost Auditing Party**") shall have the right for a period of ******** years after the date of each Development Cost Reconciliation Report to appoint at its expense an independent accountant acceptable to the other Party (the "**Cost Audited Party**"), acting reasonably, to audit the applicable records of the Cost Audited Party and its Affiliates to verify that the amounts of Development Costs shown in such Development Cost Reconciliation Report and related calculations were correctly determined. The Cost Audited Party shall, and shall cause each of its Affiliates to, make its records available for audit by such independent accountant during regular business hours at such place or places where such records are customarily kept upon ******** days written notice from the Cost Auditing Party; provided that the Cost Audited Party and its Affiliates shall not be obligated to make such records available to such accountant until such accountant has entered into a non-disclosure agreement in a form acceptable to the Cost Audited Party, acting reasonably. All records made available for audit shall be deemed to be Confidential Information of the Cost Audited Party. Such audit right shall not be exercised by the Cost Auditing Party more than once in any Calendar Year and the records of Development Costs for a given period may not be audited more than once. The results of each audit, if any, shall be binding on both Parties absent manifest error. The accountant shall report to the Cost Audited Party and the Cost Auditing Party whether there was an error in the amount of Development Costs reported by the Cost Audited Party and details concerning such error, but no other information shall be disclosed to the Cost Auditing Party. In the event there was an error in the amount of Development Costs reported by the Cost Audited Party hereunder: (i) if the amount of Development Costs was over reported, the Cost Audited Party shall promptly (but in any event no later than ******** days after the Cost Audited Party's receipt of the report so concluding) make payment to the Cost Auditing Party in an amount equal to the overpayment by, or underpayment to, the Cost Auditing Party (calculated based on the amount that would have been paid by or to the Cost Auditing Party if the Development Costs had been reported correctly); and (ii) if the amount of Development Costs was underreported, the Cost Auditing Party shall promptly (but in any event no later than ******** days after the Cost Auditing Party's receipt of the report so concluding) make payment to the Cost Audited Party in an amount equal to the overpayment by, or underpayment to, the Cost Audited Party (calculated based on the amount that would have been paid by or to the Cost Audited Party if the Development Costs had been reported correctly). The Cost Auditing Party shall bear the full cost of such audit unless such audit discloses an over reporting by the Cost Audited Party of more than ******** percent (********%) of the aggregate amount of Development Costs reportable in any Calendar Year, in which case the Cost Audited Party shall reimburse the Cost Auditing Party for all reasonable and documented costs incurred by the Cost Auditing Party in connection with such audit. Notwithstanding the foregoing, AstraZeneca shall not be obligated to maintain records with respect to, and Targacept shall have no right to audit, Unshared Development Costs incurred by AstraZeneca.

(c) Good Faith Estimate. Without limitation of Section 3.9.1, within ******** days after the end of each month, AstraZeneca shall contact Targacept's Controller and provide by email its best estimate in good faith of the Development Costs incurred by AstraZeneca in such month. AstraZeneca acknowledges that Targacept will use such good faith estimate in the preparation of its financial statements, but the Parties agree that such good faith estimate shall not have application to any provision of this Agreement and that AstraZeneca shall have no responsibility or liability with respect to Targacept's financial statements.

3.10 **Co-Promotion**. Notwithstanding anything in this Agreement to the contrary, but subject to this Section 3.10, Targacept shall have the right to designate all Licensed Products as Co-Promoted Products (the "**Co-Promotion Right**") by giving written notice to AstraZeneca at any time on or before the later of (a) ******** days after the submission of an NDA for the first Licensed Product and (b) ******** days after AstraZeneca has provided to Targacept the Amplixa Co-Promotion Information Documents. For clarity but without limitation of the last paragraph of Section 3.7.2, any period during which AstraZeneca answers Targacept's questions with respect to the Co-Promotion Information Documents shall in no way impact the foregoing deadline. Targacept shall promote in accordance with the Co-Promotion Agreement each Co-Promoted Product for all Indications for which Regulatory Approval for such Co-Promoted Product is obtained in the U.S. Territory.

3.10.1 *Negotiation of Co-Promotion Agreement*. As soon as practicable following the exercise by Targacept of its Co-Promotion Right, the Parties shall commence the preparation of a co-promotion agreement for Co-Promoted Products (the "**Co-Promotion Agreement**"), that shall: (a) set forth the terms applicable to the co-promotion in the U.S. Territory of each Licensed Product for so long as it remains a Co-Promoted Product; (b) conform in all material respects with the terms and conditions set forth on Schedule 6 attached hereto; and (c) include such additional provisions as are usual and customary for inclusion in a co-promotion agreement between companies in the pharmaceutical industry of comparable size and expertise to the respective Parties, which, for clarity, shall supplement and shall not materially expand, limit or change the terms and conditions set forth on Schedule 6 attached hereto. The Parties shall use diligent efforts in good faith to negotiate, execute and deliver the Co-Promotion Agreement within ******** days following the exercise by Targacept of the Co-Promotion Right.

3.10.2 *Breach of Co-Promotion Agreement*. For clarity, following the effective date of the Co-Promotion Agreement, if any, a determination that either Targacept or AstraZeneca (or its applicable Affiliate) has breached the Co-Promotion Agreement shall not constitute a breach of this Agreement and shall be governed solely by the terms of the Co-Promotion Agreement.

3.10.3 *Amendment to Co-Promotion Terms Under Prior Agreement*. Promptly after the execution of the Co-Promotion Agreement, if any, Targacept and AstraZeneca shall discuss in good faith any appropriate amendments to Schedule 5.11.2 to the Collaborative Research and License Agreement by and between Targacept and AstraZeneca or an Affiliate thereof dated December 27, 2005, as amended, or any co-promotion agreement entered into thereunder in light of the differences in terms between such Schedule 5.11.2 or co-promotion agreement and the Co-Promotion Agreement.

3.10.4 *Dispute Resolution*. In the event the Parties fail to negotiate, execute and deliver the Co-Promotion Agreement within the ******** day period described in Section 3.10.1, either Party may submit a list of unresolved issues for resolution pursuant to 'baseball' arbitration pursuant to Section 12.1.3.

3.11 **Backup R&D Programs Agreement**.

3.11.1 *Negotiation, Execution and Delivery.* Targacept and AstraZeneca agree to negotiate in good faith the terms and conditions pursuant to which (a) Targacept would conduct research with respect to (i) its product candidate that it refers to as ******** (or its product candidate that it refers to as ********), (ii) a ******** and ******** or ******** that are NCBs and (iii) a ******** and ******** or ******** that inhibit the activity of an NNR by occupying the site at which acetylcholine naturally accesses such NNR (clauses (i), (ii) and (iii), collectively, the "**Backup R&D Programs**") and (b) AstraZeneca would have ******** in a specified field certain compounds advanced in the Backup R&D Programs (the "**Backup R&D Programs Agreement**") as soon as reasonably practicable following the Effective Date. AstraZeneca and Targacept shall work diligently and in good faith to negotiate, execute and deliver the Backup R&D Programs Agreement within ******** days after the Effective Date. The Parties contemplate that part of the compensation to Targacept with respect to such Backup R&D Programs Agreement would be ******** paid ******** over ********-year period.

3.11.2 *Dispute Resolution.* In the event the Parties fail to negotiate, execute and deliver the Backup R&D Programs Agreement within the ******** day period described in Section 3.11.1, the Parties shall use diligent efforts to complete such negotiations and to execute and deliver the Backup R&D Programs Agreement as soon as practicable thereafter. If, notwithstanding such diligent efforts, the Parties fail to execute and deliver the Backup R&D Programs Agreement within ******** days after the Effective Date, each Party shall produce a list of unresolved issues and submit its list to the JDC to be resolved in accordance with Section 2.1.5. If, notwithstanding such diligent efforts, the Parties fail to execute and deliver the Backup R&D Programs Agreement within ******** days after the Effective Date, neither Party shall have any further obligation or liability to the other Party with respect to the Backup R&D Programs, or any of them, or the Backup R&D Programs Agreement. For clarity, if for any reason there is no Backup R&D Programs Agreement executed and delivered by both Parties, no payment made or other consideration given to Targacept under this Agreement shall be required to be refunded or returned to AstraZeneca.

3.12 **Subcontracting**.

3.12.1 *By AstraZeneca*. Unless expressly contemplated by the Amplixa Global Development Outline agreed as of the Execution Date, AstraZeneca may subcontract with a Third Party to perform any or all AstraZeneca Development Activities (other than Manufacturing Development) only with the prior written consent of Targacept, such consent not to be unreasonably withheld, conditioned or delayed. For clarity, subject to the terms of the Existing TRGT Supply Agreements and except as otherwise provided in Sections 4.5, 4.6 and 6.2.1, AstraZeneca shall have the right in its sole discretion to subcontract with a Third Party to perform any or all of its Manufacturing Development, Manufacturing or Commercialization obligations hereunder. Notwithstanding the foregoing, AstraZeneca shall not subcontract any of its rights or obligations under Article 7 with respect to the Prosecution and Maintenance, enforcement or defense of any Patent Rights licensed by USFRF to Targacept under the USFRF Agreement without the prior written consent of Targacept and USFRF.

3.12.2 *By Targacept*. Unless expressly contemplated by an Amplixa Annual Global Development Plan, Targacept may subcontract with a Third Party to perform any or all of its obligations hereunder only with the prior written consent of AstraZeneca, such consent not to be unreasonably withheld, conditioned or delayed.

3.12.3 *Subcontract Requirements*. Notwithstanding Section 3.12.1 or Section 3.12.2, (a) no otherwise permitted subcontracting shall relieve a Party of any liability or obligation hereunder and (b) the agreement pursuant to which a Party engages any Third Party subcontractor must (i) be consistent in all material respects with this Agreement, (ii) contain terms obligating such subcontractor to comply with the confidentiality provisions of this Agreement and providing the other Party with substantially the same rights with respect to any intellectual property arising from the performance of the subcontracted obligation as such other Party would have if such intellectual property had arisen from the performance of such obligation by the subcontracting Party, and (iii) contain terms obligating such subcontractor to permit the other Party rights of inspection, access and audit substantially similar to those provided to the other Party in this Agreement.

ARTICLE 4
GRANT OF RIGHTS; PROPRIETARY MATERIALS

4.1 **License Grants; Sublicenses**.

4.1.1 *Targacept License Grants*.

(a) Development Program. Subject to (i) all of the terms of this Agreement and (ii) rights of the U.S. government and rights reserved by USFRF and Yale under the Targacept Sublicense Agreements, Targacept hereby grants to AstraZeneca and its Affiliates a royalty-free, worldwide, exclusive (including as to Targacept and its Affiliates) license (or sublicense) during the Term, with the right to grant sublicenses solely as provided in Section 4.1.3 and Section 7.12.1(d), under Targacept Technology for the sole purpose of Developing Compounds and Licensed Products in the Field in the entire world.

(b) Commercialization. Subject to (i) all of the terms of this Agreement and (ii) rights of the U.S. government and rights reserved by USFRF and Yale under the Targacept Sublicense Agreements, Targacept hereby grants to AstraZeneca during the Term a royalty-bearing, worldwide, exclusive (including as to Targacept and its Affiliates) license (or sublicense), with the right to grant sublicenses solely as provided in Section 4.1.3 and Section 7.12.1(d), under Targacept Technology for the sole purpose of Commercializing Compounds and Licensed Products in the Field in the entire world.

(c) Pentad. Notwithstanding anything in this Agreement to the contrary (including the definitions), the Parties expressly acknowledge and agree that, as between the Parties, Targacept shall own all right, title and interest in and to, and no license is granted to AstraZeneca or any of its Affiliates hereunder to, and AstraZeneca shall have no right to Prosecute and Maintain any Patent Rights that claim or cover, the proprietary Information of Targacept or any of its Affiliates (including Targacept's database) concerning structure-activity relationships of compounds and NNRs or any component subunit thereof, pharmacophore mapping of NNRs or any component subunit thereof or computational or quantum mechanical methods for use in the design, synthesis and evaluation of compounds, in each case as exists on the Execution Date, during the period from the Execution Date until the Effective Date, or during the Term. For clarity, the Information and Patent Rights described in the immediately preceding sentence do not include Information specifically with respect to, or Patent Rights that claim or cover, any Compounds or Licensed Products.

4.1.2 *AstraZeneca License Grants*. Subject to all of the terms of this Agreement, AstraZeneca hereby grants to Targacept an exclusive (including as to AstraZeneca and its Affiliates), royalty-free, worldwide license, without the right to grant sublicenses, during the Term under the AstraZeneca Technology and AstraZeneca's right, title and interest in and to the Targacept Technology for the sole purpose of performing the Targacept Development Activities anywhere in the world; provided that, for purposes of this Section 4.1.2, Targacept Development Activities include all actions taken by Targacept that it reasonably and in good faith believes are permitted by this Agreement and Targacept's performance of Section 3.3.4. For clarity, the rights granted by AstraZeneca under this Section 4.1.2 are not consideration for the intellectual property rights granted by Targacept under Section 4.1.1 or elsewhere in this Agreement.

4.1.3 *Sublicensing*. Except as otherwise provided in this Section 4.1.3, AstraZeneca shall have the right to grant sublicenses under the rights granted in Section 4.1.1 through multiple tiers of Sublicensees; provided that: (a) any such sublicense is consistent with and subject to the terms of this Agreement (including this Article 4) and shall terminate automatically upon termination of the corresponding license hereunder; (b) AstraZeneca shall provide written notice to Targacept of any such sublicense and provide copies to Targacept (and, in the case of a sublicense to Targacept Technology licensed by USFRF to Targacept under the USFRF Agreement, to USFRF) of each such sublicense (with confidential and financial information redacted) promptly after the execution thereof; and (c) AstraZeneca shall not be relieved of its obligations pursuant to this Agreement as a result of such sublicense except to the extent satisfactorily performed by such Sublicensee. Notwithstanding the foregoing or any other provision of this Agreement, except as provided in Section 7.12.1(d) and except for sublicenses granted to Affiliates of AstraZeneca, neither AstraZeneca nor any Sublicensee shall have the right to grant sublicenses under any of the rights and licenses granted in Section 4.1.1 in ************ without ********. For clarity, if AstraZeneca otherwise has the right to sublicense pursuant to this Section 4.1.3, AstraZeneca shall have the right, without the consent of USFRF, to grant sublicenses through multiple tiers of Sublicensees with respect to the Targacept Technology licensed by USFRF to Targacept under the USFRF Agreement.

4.1.4 *No Implied Licenses; Retention of Rights*. Except as expressly provided herein, no license or other right is or shall be created or granted hereunder by implication, estoppel or otherwise. For clarity, notwithstanding anything in this Agreement to the contrary, Targacept retains all of its right, title and interest in and to Targacept Technology in the entire world other than the rights and licenses granted to AstraZeneca pursuant to Section 4.1.1(a) and Section 4.1.1(b) and AstraZeneca retains all of its right, title and interest in and to AstraZeneca Technology in the entire world other than the rights and licenses granted to Targacept pursuant to Section 4.1.2.

4.2 **Confirmatory Patent Licenses**. Each Party shall, if reasonably requested to do so by the other Party, promptly enter into confirmatory license agreements in the form or substantially in the form set out in Schedule 7 attached hereto for purposes of recording the licenses granted under this Agreement with such patent offices in the Territory as such first Party considers reasonably necessary, including to avoid disclosure of this Agreement. As between the Parties, regardless of whether any required confirmatory licenses are executed, the Parties' respective rights and obligations in respect of the Targacept Patent Rights, AstraZeneca Patent Rights, Targacept Program Patent Rights, AstraZeneca Program Patent Rights and Joint Program Patent Rights shall be as set forth under this Agreement.

4.3 **Indication of Licensed Status**. To the extent permitted under Applicable Laws, the packaging and labeling for each Licensed Product will indicate that the Licensed Product is licensed by AstraZeneca from Targacept in a manner to be decided by AstraZeneca in its reasonable discretion but in any case in a manner that provides Targacept's name and logo with at least reasonable prominence.

4.4 **Supply of Proprietary Materials**. From time to time during the Term, either Party may supply the other Party with Proprietary Materials of the transferring Party for use in the Development Program. In connection therewith, each Party that receives Proprietary Materials of the other Party hereby agrees that: (a) it shall not use such Proprietary Materials for any purpose other than to exercise its rights or perform its obligations hereunder; (b) it shall use such Proprietary Materials only in compliance with Article 8 and all Applicable Laws; (c) it shall not transfer any such Proprietary Materials to any Third Party without the prior written consent of the transferring Party, except as expressly permitted hereby; (d) the receiving Party shall not acquire any right, title or interest in or to such Proprietary Materials as a result of such supply by the transferring Party; and (e) at the end of the Development Program, the receiving Party shall, if and as instructed by the transferring Party and as further provided in Article 8, either destroy or return any such Proprietary Materials that are not the subject of the grant of a continuing license hereunder.

4.5 **Distributors and Net Sales Distributors**. Subject to Section 4.1.3, AstraZeneca shall have the right, in its sole discretion, to appoint any of its Affiliates, and AstraZeneca and any of its Affiliates shall have the right, in their sole discretion, to appoint any other Person or Persons, in the Territory (subject to the proviso below), to distribute, market and sell Licensed Products (with or without packaging rights), in circumstances where such Person purchases its requirements of Licensed Products from AstraZeneca or any of its Affiliates; provided that, notwithstanding the foregoing, neither AstraZeneca nor any of its Affiliates shall have such right with respect to ******** unless Targacept shall ********. Where AstraZeneca or any of its Affiliates appoints such a Person and such Person (a) is not an Affiliate of AstraZeneca, (b) does not make any royalty or other payments (e.g., upfront payment, quarterly distribution payments, etc.) with respect to intellectual property rights of AstraZeneca or any of its Affiliates or for the right to distribute Licensed Products, however characterized, to AstraZeneca, any of its Affiliates or any Third Party designated by AstraZeneca and (c) unless distributors used by AstraZeneca or its Affiliates in the ordinary course of business are responsible for promotion and advertising costs (in which event this clause (c) shall have no force or effect and be ignored), does not bear any part of the promotion or advertising costs of any such Licensed Product, such Person shall be a "**Distributor**." Where AstraZeneca or any of its Affiliates appoints such a Person and such Person (i) is not an Affiliate of AstraZeneca and (ii) either (A) makes royalty or other payments (e.g., upfront payment, quarterly distribution payments, etc.) with respect to intellectual property rights of AstraZeneca or any of its Affiliates or for the right to distribute Licensed Products, however characterized, to AstraZeneca, any of its Affiliates or any Third Party designated by AstraZeneca or (B) unless distributors used by AstraZeneca or its Affiliates in the ordinary course of business are responsible for promotion and advertising costs (in which event this clause (B) shall have no force or effect and be ignored), bears all or any part of the promotion or advertising costs of any such Licensed Product, such Person shall be a "**Net Sales Distributor**." For clarity, no Distributor is a Net Sales Distributor and no Net Sales Distributor is a Distributor. The term "packaging rights" in this Section 4.5 shall mean the right for the Distributor or Net Sales Distributor to package Licensed Products supplied in unpackaged bulk form into individual ready-for-sale packs.

4.6 **Co-Promotion Rights**. Subject to Section 4.1.3, AstraZeneca and its Affiliates shall have the right, in their sole discretion, to co-promote Licensed Products with any other Person(s) (or, solely outside of the Major Countries, to appoint one or more Third Parties to promote Licensed Products without AstraZeneca) in all or any part of the Territory; provided that (a) such co-promotion or Third Party promotion does not affect the rights of Targacept under Section 3.10 or the Co-Promotion Agreement, if any, and (b) in ******** in which such co-promotion or Third Party promotion for any Licensed Product occurs, AstraZeneca (together with its Affiliates) must itself provide at least ******** percent (********%) of ******** for Licensed Products ******** in each Calendar Quarter, unless Targacept shall have given prior written consent otherwise (not to be unreasonably withheld, conditioned or delayed). For clarity, if AstraZeneca requests that Targacept consent to an arrangement whereby AstraZeneca (together with its Affiliates) would not itself provide at least ******** percent (********%) of ******** for Licensed Products in ******** or Calendar Quarter, the withholding, conditioning or delaying of such consent by Targacept may or may not be reasonable.

4.7 **Potential Expansion of Field to Include Excluded Indications**.

4.7.1 *Targacept Notice*. If at any time Targacept or any of its Affiliates wishes to conduct any activity, either on its own, or with, for the benefit of, or sponsored by, any Third Party, that is designed to ******** or ********, or to ******** or other ******** (including any ********) to any Third Party to utilize any Information, Invention or Patent Rights Controlled by Targacept or any of its Affiliates for the purpose of ******** or ********, any Compound or Licensed Product in any Excluded Indication, Targacept shall provide AstraZeneca with ******** days' written notice prior to conducting such activity or ******** such ******** or other ********, which notice shall specify the applicable Excluded Indication, describe the reasons for Targacept's interest in conducting such activity or ******** such ******** or other ******** and include any data or information known to Targacept that supports the use of such Compound or Licensed Product for such Excluded Indication. Thereafter, Targacept shall provide AstraZeneca with such other information with respect thereto as AstraZeneca may reasonably request.

4.7.2 *AstraZeneca Option*. If Targacept provides a notice contemplated by Section 4.7.1, AstraZeneca shall have the right, upon written notice to Targacept within ******** days after receipt of such notice, to elect to expand the Field to include the Excluded Indication specified in Targacept's notice. If AstraZeneca exercises its option as provided above, such Excluded Indication shall thereupon become included in the Field (such Excluded Indication, an "**Expanded Field Indication**") effective from and after the date of AstraZeneca's notice pursuant to this Section 4.7.2; provided that, for clarity and notwithstanding anything herein to the contrary, unless AstraZeneca expressly agrees otherwise in writing, (a) AstraZeneca shall have no obligation hereunder to ******** or ******** any Compound or Licensed Product for any Expanded Field Indication and (b) Targacept shall have no right to any ******** under Section ******** (but shall, for clarity, have the right to ******** under Section ********) with respect to any Expanded Field Indication. For clarity, if AstraZeneca does not exercise its option as provided above with respect to an Excluded Indication specified in Targacept's notice, then Targacept shall be free to Develop or Commercialize any Compound or Licensed Product for such Excluded Indication.

For clarity this Section 4.7 shall have no application to any compound that is not a Compound or any product that is not a Licensed Product.

ARTICLE 5
PAYMENTS

5.1 **Upfront Payment**. AstraZeneca shall pay Targacept a non-refundable, non-creditable upfront fee in the amount of Two Hundred Million Dollars (US $200,000,000), payable by wire transfer of immediately available funds within ******** Business Days after the Effective Date according to written instructions that Targacept shall provide.

5.2 **Milestone Payments**.

5.2.1 *Development and Regulatory Milestones*. Subject to Section 5.11, AstraZeneca shall make each of the following non-refundable, non-creditable payments to Targacept within ********** days after the first occurrence of the corresponding Milestone Event; provided that, for clarity, payment with respect to each such Milestone Event shall be made only one time regardless of the number of Licensed Products that achieve such Milestone Event.

Milestone Event	Payment
******** of ******** or ******** for a Licensed Product that is ********	******** Dollars
******** of ******** for a Licensed Product that is ******** in ******** in the ******** or using the ******** in the ********	******** Dollars
******** of ******** for a Licensed Product that is ******** in ********	******** Dollars
******** of a Licensed Product that is ******** in a ******** in ********	******** Dollars
******** of ******** for a Licensed Product that is ********	******** Dollars
******** of ******** or ******** for a Licensed Product that is ********	******** Dollars
******** of ******** for a Licensed Product that is ******** in ******** in ******** or using the ******** in ********	******** Dollars
******** of ******** for a Licensed Product that is ******** or ******** in ********	******** Dollars
******** of ******** for a Licensed Product that is ******** in ********	******** Dollars
******** of a Licensed Product that is ******** in ******** in ********	******** Dollars
******** of a Licensed Product that is ******** or ******** in ********	******** Dollars
******** of ******** set forth on ******** attached hereto	******** Dollars

For clarity, in no event shall AstraZeneca pay more than 540 Million Dollars under this Section 5.2.1.

5.2.2 *Sales Milestones*. In addition to the milestone payments contemplated by Section 5.2.1, subject to Section 5.11, AstraZeneca shall make each of the following non-refundable, non-creditable payments to Targacept within ************ days after the first occurrence of the corresponding Milestone Event; provided that, for clarity, payment with respect to each such Milestone Event shall be made only one time.

Milestone Event	Payment
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars
Worldwide Net Sales of all Licensed Products ******** of at least ******** Dollars	******** Dollars

For clarity, (a) in no event shall AstraZeneca pay more than 500 Million Dollars under this Section 5.2.2 and (b) Net Sales of each Licensed Product in each country in the Territory shall be included in worldwide Net Sales for purposes of this Section 5.2.2, whether or not the Royalty Term for such Licensed Product for such country has expired.

5.2.3 *Determination that Milestone Events have Occurred*. AstraZeneca shall provide Targacept with prompt written notice upon each occurrence of each Milestone Event. In the event that, notwithstanding the fact that AstraZeneca has not given such a notice, Targacept believes any such Milestone Event has occurred, it shall so notify AstraZeneca in writing and shall provide to AstraZeneca data, documentation or other information that supports its belief. Any dispute under this Section 5.2.3 that relates to whether or not a Milestone Event has occurred shall first be referred to the JDC to be resolved in accordance with Section 2.1.5; provided that, if such dispute is not resolved in accordance with Section 2.1.5(a) or Section 2.1.5(b), it shall be subject to resolution in accordance with Section 12.1.

5.2.4 *Special Milestone*. AstraZeneca hereby agrees that, with respect to the Milestone Product for which Regulatory Approval is sought in ********, if any, it shall request the ******** to ******** the ******** of ******** to ******** the Milestone Product in ******** in a manner that would reasonably be expected to result in the achievement of the ******** set forth in item 3 on ******** attached hereto, unless either (a) the criteria set forth in item 1 on ******** attached hereto have not been achieved or (b) it could not reasonably be concluded that the ******** set forth in item 2 on ******** attached hereto have been achieved.

5.3 **Payment of Royalties; Royalty Rates; Accounting and Records**.

5.3.1 *Payment of Royalties*.

(a) Royalties Applicable in ROW Territory. Subject to Section 5.3.1(c) and Section 5.11, AstraZeneca shall pay Targacept a royalty on Net Sales of all Licensed Products in the ROW Territory (excluding Net Sales of each Licensed Product in any country in the ROW Territory for which the Royalty Term for such Licensed Product and country has expired) in each Calendar Year (or partial Calendar Year), as follows:

That portion of Net Sales of all Licensed Products in the ROW Territory in a Calendar Year that is:	**Royalty Percentage**
Not greater than ******** Dollars	********%
Greater than ******** Dollars but not greater than ******** Dollars	********%
Greater than ******** Dollars but not greater than ******** Dollars	********%
Greater than ******** Dollars	********%

(b) Royalties Applicable in the U.S. Territory. Subject to Section 5.3.1(c) and Section 5.11, AstraZeneca shall pay Targacept a royalty on Net Sales of all Licensed Products in the U.S. Territory (excluding Net Sales of each Licensed Product for which the Royalty Term for the U.S. Territory has expired) in each Calendar Year (or partial Calendar Year), as follows:

That portion of Net Sales of all Licensed Products in the U.S. Territory in a Calendar Year that is:	**Royalty Percentage**
Not greater than ******** Dollars	********%
Greater than ******** Dollars but not greater than ******** Dollars	********%
Greater than ******** Dollars but not greater than ******** Dollars	********%
Greater than ******** Dollars	********%

(c) Reduction of Royalty.

(i) *No Royalty-Bearing Claim*. With respect to a Licensed Product in a country in the Territory, from and after the expiration date in such country of the last to expire of, or during any period during the Royalty Term in such country in which there are no, Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Program Patent Rights, AstraZeneca Extended Term Patent Rights or Joint Program Patent Rights in such country that includes a Valid Claim that covers (A) the ******** of such Licensed Product, (B) a ******** or ******** such Licensed Product (including the ******** of such Licensed Product), or (C) a ******** of such Licensed Product for any ******** for which such Licensed Product has ******** (and, in the case of any country in which ******** or ******** is required, such ******** or ********) in such country if, solely in the case of this clause (C), no ******** (other than a ******** or ********of ********) is ******** in such country a ******** that (1) is, if such country is the U.S. Territory, ******** in the ******** as a ******** that the ******** to be ******** such Licensed Product or (2) is, if such country is in the ROW Territory, ******** in such country as ******** and ******** such Licensed Product in the manner required by Applicable Laws in such country, the royalty rate(s) payable to Targacept by AstraZeneca under Section 5.3.1(a) or Section 5.3.1(b), as the case may be, with respect to Net Sales of such Licensed Product in such country shall be reduced by ******** percent (********%).

For purposes of this Section 5.3.1(c)(i): (A) if the affected country is in ROW Territory, the portion of Net Sales of the affected Licensed Product in such country subject to each of the royalty rates under Section 5.3.1(a) shall be proportional to Net Sales of all Licensed Products in all countries in the ROW Territory subject to the applicable royalty rates under Section 5.3.1(a); and (B) if the affected country is the United States, the portion of Net Sales of the affected Licensed Product subject to each of the royalty rates under Section 5.3.1(b) shall be proportional to Net Sales of all Licensed Products in the U.S. Territory subject to the applicable royalty rates under Section 5.3.1(b). Schedule 12 attached hereto contains an example calculation pursuant to this Section 5.3.1(c)(i). The calculation set forth on Schedule 12 is for illustrative purposes only.

(ii) *Royalty Stacking*. Subject to Section 5.3.1(c)(iv), AstraZeneca shall have the right to reduce the amount of royalties owing to Targacept under Section 5.3.1(a) or Section 5.3.1(b), whichever one is applicable, by ******** percent (********%) of the amount of royalties (if any) and other amounts (including license fees and milestones) paid by AstraZeneca or any of its Affiliates (including on behalf of any Sublicensee, Distributor or Net Sales Distributor) to any Third Party in consideration for the license of Patent Rights for any country if, at the time such license is granted, it is more likely than not that such Patent Rights would be infringed by the Development or Commercialization of a Licensed Product in the Field for such country in the absence of such license.

For purposes of this Section 5.3.1(c)(ii), (1) if the affected country is in the ROW Territory, the portion of Net Sales of the affected Licensed Product in such country subject to each of the royalty rates under Section 5.3.1(a) shall be proportional to Net Sales of such Licensed Product in all countries in the ROW Territory subject to the applicable royalty rates under Section 5.3.1(a); and (2) if the affected country is the United States, the portion of Net Sales of the affected Licensed Product subject to each of the royalty rates under Section 5.3.1(b) shall be proportional to Net Sales of all Licensed Products in the U.S. Territory subject to the applicable royalty rates under Section 5.3.1(b).

(iii) *Compulsory Licenses*. In the event that a court or a governmental agency of competent jurisdiction requires AstraZeneca or any of its Affiliates or Sublicensees to grant a compulsory license to a Third Party permitting such Third Party to make and sell a Licensed Product in a country in the Territory and such Third Party in fact makes and sells such Licensed Product in such country, then, for the purposes of calculating the royalties payable with respect to such Licensed Product under Section 5.3.1(a) or Section 5.3.1(b), as the case may be, ******** percent (********%) of the Net Sales of such Licensed Product in such country shall be disregarded for so long as such Third Party in fact makes and sells such Licensed Product in such country, subject to Section 5.3.1(c)(iv).

(iv) *Application of Reductions*. (A) In no event shall the royalties owed under Section 5.3.1(a) with respect to Net Sales of a Licensed Product in a particular country in the ROW Territory in any Calendar Quarter after giving effect to any required adjustment pursuant to Section 5.3.1(c)(i) be reduced by operation of Sections 5.3.1(c)(ii) and 5.3.1(c)(iii), together, by more than ******** percent (*********%) of what would otherwise be owed under Section 5.3.1(a) with respect to Net Sales of such Licensed Product in such country in such Calendar Quarter after giving effect to any required adjustment pursuant to Section 5.3.1(c)(i). In no event shall the royalties owed under Section 5.3.1(b) for any Calendar Quarter after giving effect to any required adjustment pursuant to Section 5.3.1(c)(i) be reduced by operation of Sections 5.3.1(c)(ii) and 5.3.1(c)(iii), together, by more than ******** percent (*********%) of what would otherwise be owed under Section 5.3.1(b) for such Calendar Quarter after giving effect to any required adjustment pursuant to Section 5.3.1(c)(i). Reductions under Section 5.3.1(c), together with reductions under Section 6.2.1, not exhausted in any Calendar Quarter may be carried into future Calendar Quarters.

(v) *Effect of Expiration of Royalty Term*. With respect to each Licensed Product in each country in the Territory, from and after the expiration of the Royalty Term for such Licensed Product in such country, Net Sales of such Licensed Product in such country shall be excluded for purposes of calculating the royalty thresholds and ceilings set forth in Section 5.3.1(a) or Section 5.3.1(b), as the case may be.

(d) Payment Dates and Reports. Royalty payments shall be made by AstraZeneca within ******** days after the end of each Calendar Quarter commencing with the Calendar Quarter in which the first day of the first Royalty Term for the first Licensed Product occurs. AstraZeneca shall also provide, at the same time each such payment is made, a report showing: (i) the Net Sales of Licensed Products by country in the Territory; (ii) the basis for any deductions from gross amounts billed or invoiced to determine Net Sales; (iii) the applicable royalty rates for Licensed Products; (iv) the exchange rates used in calculating any of the foregoing; (v) a calculation of the amount of royalty due to Targacept; and (vi) such additional information as Targacept may be required to provide to USFRF under the USFRF Agreement or to Yale under the Yale Agreement.

(e) Acknowledgement of Blended Royalty. The Parties hereby acknowledge and agree that royalties may become payable hereunder for each Licensed Product for which there are no Targacept Patent Rights or Targacept Program Patent Rights and that such royalties are in consideration of each of the following, separately and together, which have substantial economic benefit to AstraZeneca: (i) Targacept's expertise and know-how relating to NNRs; (ii) the disclosure by Targacept to AstraZeneca of Preclinical Activities and Clinical Studies conducted with the Primary Compound, as well as results obtained in the Development Program; (iii) the licenses granted to AstraZeneca hereunder with respect to Targacept Technology that is not within the claims of any Targacept Patent Rights or Targacept Program Patent Rights; (iv) the restrictions on Targacept pursuant to Section 6.1; and (v) the benefit afforded to AstraZeneca by each of the foregoing. The Parties agree that the royalty rates set forth herein reflect an efficient and reasonable blended allocation of the values provided by Targacept to AstraZeneca.

5.4 **Diagnostic or Veterinary Products**. The milestones and royalties in Sections 5.2 and 5.3 shall not apply to Development and Commercialization of Licensed Products for diagnostic or veterinary use, or for uses solely for screening patients who have been diagnosed with a disease, state or condition for eligibility to be treated for such disease, state or condition with a Licensed Product or for monitoring patients who are or have been treated with a Licensed Product. In the event that a Licensed Product is Developed for commercial diagnostic or veterinary purposes, the Parties shall negotiate a downward adjustment to such milestones and royalties for the sale of such Licensed Product that reflects the commercial potential of such Licensed Product and standard commercial terms in the industry for diagnostic or veterinary products, as applicable.

5.5 **Records; Royalty Audit Rights**. AstraZeneca shall, and shall cause its Affiliates and its and their Sublicensees and Net Sales Distributors to, keep and maintain for ********years from the date of each payment of royalties hereunder complete and accurate records of gross sales and Net Sales by AstraZeneca and its Affiliates and its and their Sublicensees and Net Sales Distributors of each Licensed Product, in sufficient detail to allow royalties under Section 5.3 (and the related financial obligations under the Targacept Sublicense Agreements) to be determined accurately. Targacept shall have the right for a period of ******** years after receiving any such payment to appoint at its expense, subject to the last sentence of this Section 5.5, an independent accountant acceptable to AstraZeneca, acting reasonably, to audit the applicable records of AstraZeneca and its Affiliates and its and their Sublicensees and Net Sales Distributors to verify that such amounts were correctly determined. AstraZeneca shall, and shall cause each of its Affiliates and each of their respective Sublicensees and Net Sales Distributors to, make its records available for audit by such independent accountant during regular business hours at such place or places where such records are customarily kept, upon ******** days written notice from Targacept; provided that neither AstraZeneca nor any of its Affiliates nor any of their respective Sublicensees or Net Sales Distributors shall be obligated to make such records available to such accountant until such accountant has entered into a non-disclosure agreement in a form acceptable to AstraZeneca, acting reasonably. All records made available for audit shall be deemed to be Confidential Information of AstraZeneca. Such audit right shall not be exercised by Targacept more than ******** in any Calendar Year or more than ******** with respect to amounts payable in a particular period. The results of each audit, if any, shall be binding on both Parties absent manifest error. The accountant shall report to AstraZeneca and Targacept whether the royalty reports are correct and details concerning any discrepancies, but no other information shall be disclosed to Targacept. In the event there was an underpayment by AstraZeneca hereunder, AstraZeneca shall promptly (but in any event no later than ******** days after AstraZeneca's receipt of the report so concluding) make payment to Targacept of the shortfall, and, in the event there was an overpayment by AstraZeneca hereunder, Targacept shall promptly (but in any event no later than ******** days after Targacept's receipt of the report so concluding) make payment to AstraZeneca of the overage. Targacept shall bear the full cost of such audit unless such audit discloses an underreporting by AstraZeneca of more than ******** percent (********%) of the aggregate amount payable for any Calendar Quarter, in which case AstraZeneca shall reimburse Targacept for all reasonable and documented costs incurred by Targacept in connection with such audit.

5.6 **Overdue Royalties and Milestones**. All royalty payments not made within the time period set forth in Section 5.3.1(d) including underpayments discovered during an audit, and all milestone payments not made within the time period specified in Section 5.2, shall bear interest at an annual rate of LIBOR plus ************ basis points from the due date until paid in full or, if less, the maximum interest rate permitted by Applicable Laws. Any such overdue royalty or milestone payment shall, when made, be accompanied by, and credited first to, all interest so accrued. This Section 5.6 shall be in addition to any rights or remedies to which a Party may be entitled in law or equity as a result of such late payment, underpayment or failure to pay.

5.7 **Payments**. All payments made by a Party under this Article 5 shall be made by wire transfer in Dollars in accordance with instructions given in writing from time to time by the receiving Party and shall be free and clear of any taxes, duties, levies, fees or charges (including wire or other transfer fees), except as expressly provided in Section 5.9 or Section 5.10.

5.8 **Foreign Currency Exchange**. All royalty payments made under this Article 5 shall be payable in the United States in Dollars, regardless of the countries in which sales are made. In the case of Net Sales outside the United States, such currency shall be converted from local currency to United States Dollars by AstraZeneca in accordance with the rates of exchange for the relevant month for converting such other currency into Dollars used by AstraZeneca's internal accounting systems, which AstraZeneca represents to Targacept are independently audited on an annual basis. All milestone payments shall similarly be payable in Dollars, regardless of the country in which the milestone event is achieved.

5.9 **Withholding Taxes**. The royalties, milestones and other amounts payable by AstraZeneca to Targacept pursuant to this Agreement ("**Payments**") shall not be reduced on account of any taxes unless required to be so reduced by Applicable Laws. Targacept alone shall be responsible for paying any and all taxes (other than withholding taxes required by Applicable Laws to be paid by AstraZeneca) levied on account of, or measured in whole or in part by reference to, any Payment it receives. AstraZeneca shall deduct or withhold from the Payments any taxes that it is required by Applicable Laws to deduct or withhold. Notwithstanding the foregoing, if Targacept is entitled under any applicable tax treaty to a reduction of rate of, or the elimination of, applicable withholding tax, it may deliver to AstraZeneca or the appropriate governmental authority (with the assistance of AstraZeneca to the extent reasonably required and expressly requested in writing) the prescribed forms necessary to reduce the applicable rate of withholding or to relieve AstraZeneca of its obligation to withhold tax and AstraZeneca shall apply the reduced rate of withholding, or dispense with withholding, as the case may be; provided that AstraZeneca has received evidence, in a form satisfactory to AstraZeneca, of Targacept's delivery of all applicable forms (and, if necessary, its receipt of appropriate governmental authorization) at least ******** Business Days prior to the date that the applicable Payment is due. If, in accordance with the foregoing, AstraZeneca withholds any amount, it shall pay to Targacept the balance when due, make timely payment to the proper taxing authority of the withheld amount, and send to Targacept proof of such payment within ******** days following such payment.

5.10 **Indirect Taxes**. Notwithstanding anything contained in Section 5.9, this Section 5.10 shall apply with respect to Indirect Taxes. All Payments are exclusive of Indirect Taxes. If any Indirect Taxes are chargeable in respect of any Payment, AstraZeneca shall pay such Indirect Taxes at the applicable rate in respect of such Payment following the receipt, where applicable, of an Indirect Taxes invoice in the appropriate form issued by Targacept in respect of such Payment, such Indirect Taxes to be payable on the due date of the payment of the Payments to which such Indirect Taxes relate. Upon the express request by either Party, the other Party shall cooperate in all reasonable respects to issue invoices consistent with Indirect Tax requirements for any or all amounts payable under this Agreement.

5.11 **Certain Reductions for Additional Development Costs.**

5.11.1 *Initial Development Costs*. Notwithstanding anything in this Agreement to the contrary, if Targacept elects to terminate its obligation to fund any Initial Development Costs in excess of the Targacept Initial Development Cost Threshold then in effect, the amounts otherwise payable thereafter by AstraZeneca to Targacept under Section 5.2 or 5.3 (as may be adjusted pursuant to Section 5.3.1(c) or Section 6.2.1) shall automatically be reduced by the total amount of the Excess Initial Development Costs Offset for which a reduction under this Section 5.11.1 has not been made, except that in no event shall any such amount be reduced to an amount that is less than ******** (********%) of the amount that would be payable by AstraZeneca without regard to this Section 5.11.1 and without regard to Section 5.11.2. "**Excess Initial Development Costs Offset**" means an amount equal to the product of (a) ********, multiplied by (b) the difference between (i) the product of (A) the aggregate amount of Initial Development Costs (excluding Initial Development Costs that are Unshared Development Costs) incurred by both Parties multiplied by (B) ******** percent (********%), less (ii) the final Targacept Initial Development Cost Threshold as provided in Section 3.9.1(b)(iii). If a reduction under this Section 5.11.1 does not exhaust the Excess Initial Development Costs Offset, the remaining Excess Initial Development Costs Offset may be carried forward to reduce in accordance with this Section 5.11.1 amounts otherwise payable by AstraZeneca to Targacept under Section 5.2 or 5.3 (as may be adjusted pursuant to Section 5.3.1(c) or Section 6.2.1) in future periods until exhausted.

5.11.2 *Additional Development Costs*. Notwithstanding anything in this Agreement to the contrary, with respect to each Additional Development Project, if the Targacept Additional Development Cost Threshold for such Additional Development Project is $******** or if Targacept elects to terminate its obligation to fund any Additional Development Costs for such Additional Development Project in excess of the applicable Targacept Additional Development Cost Threshold then in effect, from and after the first to occur of receipt of the Additional Development Cost Offset Approval with respect to such Additional Development Project, the amounts otherwise payable by AstraZeneca to Targacept under Section 5.2 or 5.3 (as may be adjusted pursuant to Section 5.3.1(c) or Section 6.2.1) shall automatically be reduced by the total amount of the Excess Additional Development Costs Offset with respect to such Additional Development Project for which a reduction under this Section 5.11.2 has not been made, except that in no event shall any payment by AstraZeneca be reduced to an amount that is less than ******** (********%) of the amount that would be payable by AstraZeneca without regard to Section 5.11.1 and without regard to this Section 5.11.2. "**Excess Additional Development Costs Offset**" means, with respect to each Additional Development Project, an amount equal to the product of (a) ********, multiplied by (b) the difference between (i) the product of (A) the aggregate amount of Additional Development Costs with respect to such Additional Development Project (excluding Additional Development Costs that are Unshared Development Costs) incurred by both Parties multiplied by (B) ******** percent (********%), less (ii) the final Targacept Additional Development Cost Threshold with respect to such Additional Development Project as provided in Section 3.9.1(c)(iv). If a reduction under this Section 5.11.2 does not exhaust the Excess Additional Development Costs Offset, the remaining Excess Additional Development Costs Offset may be carried forward to reduce in accordance with this Section 5.11.2 the amounts otherwise payable by AstraZeneca to Targacept under Section 5.2 or 5.3 (as may be adjusted pursuant to Section 5.3.1(c) or Section 6.2.1) under this Agreement in future periods until exhausted.

ARTICLE 6
EXCLUSIVITY; STANDSTILL; TARGACEPT SUBLICENSE AGREEMENTS

6.1 **Exclusivity; Standstill**.

6.1.1 *Exclusivity*. Subject to Section 6.1.2, except in the Development or Commercialization of Compounds or Licensed Products pursuant to this Agreement, from the Effective Date until the third (3rd) anniversary thereof (the "**Exclusivity Period**"): (a) neither Party shall, and each Party shall cause its Affiliates not to, conduct a Phase 2 Clinical Trial, Phase 3 Clinical Trial or Phase 4 Clinical Trial of, or commercialize in any respect, a compound as an augmentation (add-on) or adjunctive treatment (or other term reflecting the concurrent use of two or more pharmaceutical products) for the Target Indication; and (b) neither Party shall, and each Party shall cause its Affiliates not to, grant a license (other than, in the case of Targacept, as may be provided for by the terms of the Existing TRGT Alliance Agreement in effect as of the Execution Date, whether or not the Existing TRGT Alliance Agreement is amended after the Execution Date) under any Information, Invention or Patent Rights to a Third Party to conduct a Phase 2 Clinical Trial, Phase 3 Clinical Trial or Phase 4 Clinical Trial of, or commercialize in any respect, a compound as an augmentation (add-on) or adjunctive treatment (or other term reflecting the concurrent use of two or more pharmaceutical products) for the Target Indication; provided that, notwithstanding the foregoing, the research, development, commercialization or other exploitation by AstraZeneca or its Affiliates or any licensee thereof of (i) any pharmaceutical or medicinal item, substance or formulation that is comprised of or contains quetiapine, whether or not the sole active pharmaceutical ingredient thereof, (ii) ******** known as of the Execution Date as ******** in ******** or (iii) any product from the drug class known as atypical antipsychotics that is ******** in the Territory as of ********, in each case (clauses (i), (ii) and (iii)) shall not be deemed to breach or violate this Section 6.1.1.

6.1.2 *Acquisitions or Changes of Control.*

(a) Notwithstanding Section 6.1.1, if during the Exclusivity Period, a Change of Control of Targacept occurs and the surviving or acquiring entity in such transaction is engaged in an activity that would otherwise constitute a breach of Section 6.1.1 (such activity, a "**Competitive Activity**"), neither such transaction nor the continuation of such Competitive Activity in any respect following consummation of such transaction shall constitute a breach of Section 6.1.1.

(b) Notwithstanding Section 6.1.1, if during the Exclusivity Period AstraZeneca or any of its Affiliates merges or consolidates with, or otherwise acquires or is acquired by, a Third Party (including through a Change of Control) that is engaged in a Competitive Activity, unless the Parties agree otherwise in writing, AstraZeneca or its successor (in either case, the "**Surviving Party**") shall, within ******** days after the date of such merger, consolidation or acquisition, notify Targacept in writing whether it intends to: (i) terminate, or cause its relevant Affiliate to terminate, the Competitive Activity; or (ii) divest, or cause its relevant Affiliate to divest, each compound or product that is the subject of such Competitive Activity (each such compound or product, a "**Competitive Product**").

(c) If the Surviving Party notifies Targacept in writing within such ******** day period that it intends to terminate, or cause its relevant Affiliate to terminate, such Competitive Activity, the Surviving Party or its Affiliate, shall: (i) promptly terminate such Competitive Activity as quickly as possible, with due regard for patient safety and Applicable Laws, and in any event within ******** days after the Surviving Party delivers such written notice to Targacept; provided that, notwithstanding the foregoing, with respect to any Competitive Activity that is a human clinical trial, the Surviving Party or its Affiliate shall be permitted to continue to conduct such trial, in accordance with its protocol as in effect as of the date of such notice, to completion; and (ii) confirm to Targacept in writing when such termination has been completed.

(d) If the Surviving Party notifies Targacept in writing within such thirty (30)-day period that it intends to divest all Competitive Products, the Surviving Party or its relevant Affiliate shall: (i) use diligent efforts to effect such divestiture as quickly as possible and in any event within ******** days after the Surviving Party delivers such written notice to Targacept; and (ii) confirm to Targacept in writing when such divestiture has been completed. If the Surviving Party or its relevant Affiliate fails to complete such divestiture within such ******** day-period, but can demonstrate to Targacept's reasonable satisfaction that it used diligent efforts to effect such divestiture within such ******** day period, then, unless otherwise required by Applicable Laws, such ******** day period shall be extended for such additional reasonable period thereafter as is necessary to enable such Competitive Products to be in fact divested, not to exceed an additional ******** days (or such longer period as is necessary to obtain any governmental or regulatory approvals required to complete such divestiture). The Surviving Party shall keep Targacept reasonably informed of its efforts and progress in effecting such divestiture until it is completed. If the Surviving Party or its relevant Affiliate effects such divestiture by way of one or more licenses or sublicenses, the licensor shall be entitled to receive license fees, milestones and royalties on sales of any such Competitive Product so divested; provided that neither the Surviving Party nor any of its Affiliates funds or continues to conduct in any respect the commercialization of such Competitive Product and, for clarity, such license fees, milestones or royalties shall not be a factor in determining Commercially Reasonable Efforts under this Agreement.

(e) If the Surviving Party fails to provide the notice contemplated by Section 6.1.2(c) or Section 6.1.2(d) within such ******** day period or, having provided such notice, fails to carry out the termination or divestiture, as the case may be, within the time periods required under Section 6.1.2(c) or Section 6.1.2(d), as the case may be, then, unless the Parties agree otherwise, the Surviving Party shall be deemed to be in material breach of this Agreement.

6.1.3 *Standstill*.

(a) Restrictions. Except (x) with the written consent of Targacept (which may be withheld by Targacept at the sole discretion of its Board of Directors) or (y) by way of stock dividends or other distributions made to Targacept's stockholders generally, AstraZeneca agrees that, during the period from the Effective Date until the ******** anniversary thereof, but subject to Section 6.1.3(b), AstraZeneca shall not and shall not assist or encourage others to, and shall cause its Affiliates to not and to not assist or encourage others to:

(i) acquire, publicly disclose an intention to acquire, offer or propose to acquire, solicit an offer to sell or agree to acquire, directly or indirectly, by purchase, by gift, by joining a partnership, limited partnership, syndicate or other group or otherwise, any direct or indirect beneficial or record ownership of any shares of common stock or other voting securities, or any other securities convertible into, exchangeable for or exercisable for common stock or other voting securities, of Targacept or any Controlling Affiliate thereof (all such securities, collectively, "**Voting Securities**"); provided, however, that this Section 6.1.3(a)(i) shall not prohibit: (A) AstraZeneca or its Affiliates from proposing other collaborative research agreements or license agreements to Targacept or any Affiliate thereof; or (B) AstraZeneca and its Affiliates, collectively, from acquiring, beneficially or of record, up to an aggregate number of Voting Securities that at the time of such acquisition represents (on a common stock equivalent basis), together with all Voting Securities owned by AstraZeneca and its Affiliates immediately prior to such acquisition (on a common stock equivalent basis), ******** percent (********%) or less of the number of shares of common stock outstanding of Targacept or such Controlling Affiliate, as the case may be;

(ii) participate in the formation of any person or group for the purpose of owning or acquiring Voting Securities or join with any person or group that seeks to acquire beneficial ownership of Voting Securities;

(iii) solicit, or participate in any "solicitation" of "proxies" or become a "participant" in any "solicitation in opposition" (as such terms are defined or used in Regulation 14A under the Exchange Act) with respect to Targacept or any Controlling Affiliate thereof;

(iv) initiate, propose or otherwise solicit stockholders for the approval of one or more stockholder proposals with respect to Targacept or any Controlling Affiliate thereof or induce any other person to initiate any stockholder proposal;

(v) seek to place any individual on the Board of Directors of Targacept or any Controlling Affiliate thereof;

(vi) deposit any Voting Securities in a voting trust or subject any Voting Securities to a voting agreement or other agreement or arrangement with respect to the voting of such Voting Securities;

(vii) otherwise act, alone or in concert with others, to seek to control the management, Board of Directors, policies or affairs of Targacept or any Controlling Affiliate thereof;

(viii) solicit, propose, seek to effect or negotiate with any other person (including, without limitation, Targacept or any Affiliate thereof) with respect to the acquisition of any material portion of the consolidated assets of Targacept and its Affiliates with respect to which AstraZeneca does not have a license or an option to obtain a license or any form of merger, consolidation or other form of business combination or other similar extraordinary transaction with Targacept or any Controlling Affiliate thereof or any share exchange, reorganization, recapitalization or other similar extraordinary transaction not in the ordinary course of business with respect to Targacept or any Controlling Affiliate thereof, or solicit, make or propose or negotiate with any other person with respect to, or publicly disclose an intent to make, any tender offer or exchange offer for any securities of Targacept or any Controlling Affiliate thereof, or publicly disclose an intent, purpose, plan or proposal to engage, with respect to Targacept, any Controlling Affiliate thereof, any securities of Targacept or any Controlling Affiliate thereof or any material portion of the consolidated assets of Targacept and its Affiliates with respect to which AstraZeneca does not have a license or an option to obtain a license, in any action that is described in the foregoing provisions of this Section 6.1.3(a) or that would violate the provisions of this Section 6.1.3(a), or assist, participate in, facilitate or solicit any effort or attempt by any person to do so or seek to do any of the foregoing; provided, however, that this Section 6.1.3(a)(viii) shall not prohibit AstraZeneca or its Affiliates from proposing other collaborative research agreements or license agreements with Targacept or any Affiliate thereof; or

(ix) request publicly (or in any manner that would require Targacept or any Affiliate thereof to make a public disclosure) Targacept, any Affiliate of Targacept or any of their respective directors, officers, employees or agents to amend, waive or modify any provision of this Section 6.1.3(a) or otherwise seek publicly (or in any manner that would require Targacept or any Affiliate thereof to make a public disclosure) any amendment or modification to or waiver of any obligations of AstraZeneca under this Section 6.1.3(a).

Nothing in clauses (i) through (ix) above in this Section 6.1.3(a) shall preclude or limit AstraZeneca or any Affiliate thereof from: (A) consulting on a confidential basis with Third Party advisors with respect to any proposal with respect to any transaction of the type referred to in this Section 6.1.3(a); (B) making requests to Targacept, any Affiliate of Targacept or any of their respective directors, officers, employees or agents to amend, waive or modify any provision of this Section 6.1.3(a); or (C) making or submitting to Targacept, any Affiliate of Targacept or any of their respective directors, officers, employees or agents proposals relating to possible transactions; in the case of clauses (B) and (C) above, only to the extent that such request or proposal is both non-public and not made in a manner that would require Targacept or any Affiliate thereof to make a public disclosure.

(b) Exception to Standstill Provisions. Subject to the proviso appearing beneath clause (iv) below, the restrictions of Section 6.1.3(a) shall cease to apply:

(i) if Targacept or any Controlling Affiliate thereof announces publicly a decision of its Board of Directors to conduct a formal process for the purpose of soliciting offers relating to an Acquisition Transaction (as defined in Section 6.1.3(b)(ii));

(ii) if Targacept or any Controlling Affiliate thereof enters into a definitive written agreement, written agreement in principle or written letter of intent with any party or parties (other than AstraZeneca or its Affiliates) providing for: (A) the direct or indirect sale of a number of Voting Securities that at the time of such sale represents (on a common stock equivalent basis) more than ******** percent (********%) of the number of shares of common stock outstanding of Targacept or such Controlling Affiliate, as the case may be, to any person or group that is not affiliated with AstraZeneca and its Affiliates; (B) a merger, consolidation or other form of business combination, share exchange, reorganization, recapitalization or other similar extraordinary transaction involving Targacept or such Controlling Affiliate that, if consummated, would result in the holders of the outstanding Voting Securities (on a common stock equivalent basis) of Targacept (or, if Targacept has a Controlling Affiliate, such Controlling Affiliate and not Targacept) immediately prior to such transaction ceasing to hold at least ******** percent (********%) of the combined voting power of the surviving, purchasing or continuing entity immediately after such transaction; or (C) the sale of all or substantially all of the consolidated assets of Targacept and its Affiliates to a Third Party (each of clauses (A), (B) and (C) above, an "**Acquisition Transaction**");

(iii) if any Third Party commences a tender or exchange offer which, if successful, would result in such Third Party beneficially owning not less than ******** percent (********%) of all outstanding Voting Securities (on a common stock equivalent basis) of Targacept or any Controlling Affiliate thereof and such Third Party offer is not withdrawn or terminated within ******** Business Days after its commencement; provided that, if the Board of Directors of Targacept or such Controlling Affiliate, as the case may be, (1) makes a public statement recommending the Third Party offer to the stockholders of Targacept or such Controlling Affiliate during such ******** Business Day period, then such ******** Business Day period shall expire on the date of such announcement or (2) ********, then such ******** Business Day period shall expire on the ******** Business Day of such ******** Business Day period conditional on AstraZeneca or any of its Affiliates not publicly disclosing any offer to acquire Voting Securities until at least ******** Business Days following the commencement of the Third Party offer; and provided further that, if the Board of Directors of Targacept or such Controlling Affiliate has publicly announced within ******** Business Days following the commencement of the Third Party offer that it is rejecting the Third Party offer or recommending that the stockholders of Targacept or such Controlling Affiliate do not tender and if Targacept or such Controlling Affiliate or any of their respective Boards of Directors thereafter requests, AstraZeneca shall, and shall cause its Affiliates to, cease and (unless impossible) rescind any action taken by AstraZeneca or any of its Affiliates that, but for this Section 6.1.3(b), would be prohibited by this Agreement, but only if and at such time as such Third Party withdraws or terminates its offer prior to its completion, and the restrictions in Section 6.1.3(a) shall thereupon automatically be reinstated and be in full force and effect (subject, again, to the provisions of this Section 6.1.3(b)); or

(iv) if the Board of Directors of Targacept or any Controlling Affiliate thereof adopts a plan of liquidation or dissolution;

provided that AstraZeneca and Targacept expressly agree that the termination of the obligations under Section 6.1.3(a) pursuant to this Section 6.1.3(b) shall only occur if, in connection with the applicable event set forth in this Section 6.1.3(b), there is and has been no breach by AstraZeneca or any of its Affiliates of the restrictions set forth in Section 6.1.3(a).

(v) Definitions. As used in this Section 6.1.3, “group” and “person” have the respective meanings set forth or referenced in the definition of “Change of Control.”

(c) Interpretation. For all purposes of this Section 6.1.3, the term Voting Securities shall also include any securities of Targacept or any Controlling Affiliate thereof entitled to vote generally for the election of directors of Targacept or such Controlling Affiliate that the holders of Voting Securities shall receive or as a matter of right be entitled to receive as a result of (i) any capital reorganization, recapitalization or reclassification of the capital stock of Targacept or such Controlling Affiliate or (ii) any merger, consolidation or other form of business combination, share exchange or similar extraordinary transaction of Targacept or such Controlling Affiliate with another entity in which Targacept or such Controlling Affiliate survives after such merger, consolidation or other form of business combination, share exchange or similar extraordinary transaction.

6.2 **Targacept Sublicense Agreements**.

6.2.1 *USFRF Agreement*. The sublicenses granted by Targacept to AstraZeneca under Section 4.1.1 shall terminate, solely with respect to Targacept Technology licensed by Targacept under the USFRF Agreement, upon termination of the USFRF Agreement; provided that, notwithstanding the foregoing, AstraZeneca may elect to continue such sublicenses with respect to Targacept Technology licensed by Targacept under the USFRF Agreement by advising USFRF in writing, within ******** days of AstraZeneca’s receipt of written notice of such termination from USFRF, of its election and its agreement to assume all of the obligations to USFRF (including obligations for payment) contained in the USFRF Agreement. In addition, any sublicense agreement entered into by AstraZeneca in accordance with Section 4.1.3 shall contain provisions corresponding to those of this paragraph. AstraZeneca shall have the right to reduce the amount of royalties owing to Targacept under Sections 5.3.1(a) and 5.3.1(b) (as such royalties may be adjusted pursuant to the provisions of Section 5.3.1(c)) by ******** percent (********%) of the amount of royalties (if any), or other amounts (including license fees and milestones) paid by AstraZeneca to USFRF in the event that AstraZeneca assumes all of Targacept’s obligations to USFRF under the USFRF Agreement pursuant to this Section 6.2.1.

6.2.2 *Yale Agreement*. AstraZeneca hereby: (a) assumes the same obligations of confidentiality with respect to Yale's "Confidential Information" (as defined in the Yale Agreement) that Targacept has under the Yale Agreement; (b) agrees that, with respect to any Licensed Product that is a "Licensed Product" (as defined in the Yale Agreement), AstraZeneca shall mark such Licensed Product with the numbers of all issued patents included in the Targacept Patent Rights that are sublicensed from Yale and that cover such Licensed Product in a manner that conforms with Applicable Laws in the country in which such Licensed Product is made, sold, used or shipped; (c) agrees that it shall not use the name "Yale" or "Yale University," or any variation or adaptation thereof, or any trademark, tradename or other designation owned by Yale, or the names of any of its trustees, officers, faculty, students, employees or agents, for any purpose without the prior written consent of Yale in each instance, except that AstraZeneca may state that it has sublicensed from Yale one or more of the Targacept Patent Rights; and (d) acknowledges that, upon termination of the Yale Agreement (but not expiration of its term), Yale has the option, in its discretion, of terminating the sublicenses granted by Targacept to AstraZeneca under Section 4.1.1 with respect to Targacept Technology licensed by Targacept under the Yale Agreement.

6.2.3 *USFRF and Yale*. AstraZeneca acknowledges that it has received each Targacept Sublicense Agreement and, without limiting the generality of and notwithstanding any other provision hereof, agrees that all rights and licenses granted to AstraZeneca or otherwise arising hereunder with respect to the subject matter of such Targacept Sublicense Agreement shall be subject in all respects to the rights of USFRF under the USFRF Agreement and Yale under the Yale Agreement.

6.2.4 *Financial Obligations Under Targacept Sublicense Agreements*. Notwithstanding anything in this Agreement to the contrary, but without intending to limit, modify or affect in any respect the provisions of Article 10 hereof, Targacept shall be solely responsible for all payments owed to any Third Party under the Targacept Sublicense Agreements.

6.2.5 *Standby License from Yale*. At the request of AstraZeneca at any time during the Term, Targacept shall use diligent efforts to facilitate AstraZeneca's entering into an agreement with Yale pursuant to which, in the event that the Yale Agreement is terminated, Yale would grant AstraZeneca a license to the Targacept Patent Rights that Targacept has licensed from Yale.

ARTICLE 7
INTELLECTUAL PROPERTY RIGHTS

7.1 **Targacept Intellectual Property Rights**. Targacept shall have sole and exclusive ownership of all right, title and interest on a worldwide basis in and to any and all Targacept Program Inventions, Targacept Program Patent Rights, Product Invention-Related Information, Targacept Know-How and Targacept Patent Rights. AstraZeneca agrees to assign, and hereby assigns, to Targacept all right, title and interest that AstraZeneca may acquire from time to time in any and all Product Invention-Related Information, Targacept Program Inventions and Targacept Program Patent Rights and shall, at Targacept's reasonable expense, execute all documents and do all proper actions reasonably required by Targacept from time to time to perfect Targacept's title to and ownership thereof.

7.2 **AstraZeneca Intellectual Property Rights**. AstraZeneca shall have sole and exclusive ownership of all right, title and interest on a worldwide basis in and to any and all AstraZeneca Program Inventions, AstraZeneca Program Patent Rights, AstraZeneca Know-How and AstraZeneca Patent Rights.

7.3 **Joint Intellectual Property Rights**. AstraZeneca and Targacept shall jointly own all Joint Program Information, Joint Program Inventions and Joint Program Patent Rights. The Parties hereby agree that, except to the extent restricted by Section 6.1 or any other provision of this Agreement, either Party may use or license or sublicense to any of its Affiliates or to Third Parties all or any portion of its interest in Joint Program Information, Joint Program Inventions and Joint Program Patent Rights or Confidential Information related to Joint Program Inventions, without the prior written consent of the other Party and without the obligation to provide an accounting or compensation to the other Party. Each Party shall execute all documents and do all proper actions reasonably required to fully effect the joint ownership provided for in this Section 7.3.

7.4 **Patent Coordinators**. Targacept and AstraZeneca shall each appoint a patent coordinator reasonably acceptable to the other Party (each, a "**Patent Coordinator**") to serve as such Party's primary liaison with the other Party on matters relating to Prosecution and Maintenance and enforcement of Patent Rights. Each Party may replace its Patent Coordinator at any time by notice in writing to the other Party. The initial Patent Coordinators shall be:

For Targacept: ********** (Prosecution and Maintenance only) and General Counsel (Enforcement)

For AstraZeneca: **********

7.5 **Patent-Related Matters**.

7.5.1 *Decision-Making*. With respect to each Patent-Related Matter, the Patent Coordinators, in consultation with patent counsel (provided that such consultation shall not be required with respect to any Patent Coordinator who is a patent counsel), shall use diligent efforts in good faith to determine or resolve such Patent-Related Matter at least ************ days, or such different number of days as the Patent Coordinators shall expressly agree in writing, before any action with respect to such Patent-Related Matter must be taken to be effective under applicable patent laws, regulations or administrative process in the applicable country or jurisdiction (such deadline for determination or resolution, the "**Patent-Related Matter Resolution Deadline**"); provided that, with respect to each Patent-Related Matter and unless the Parties otherwise agree, if such Patent-Related Matter has not been resolved pursuant to this Section 7.5 by the date any action with respect to such Patent-Related Matter must be taken to be effective under applicable patent laws, regulations or administrative process in the applicable country or jurisdiction (such date, the "**Patent-Related Matter Deadline**"), AstraZeneca shall, to the extent permitted under applicable patent laws, regulations or administrative process in the applicable country or jurisdiction, (a) seek an extension of such Patent-Related Matter Deadline sufficient to resolve such Patent-Related Matter by the applicable Patent-Related Matter Deadline as so extended and (b) file, if the extension contemplated by clause (a) above is not permitted under applicable patent laws, regulations or administrative process in the applicable country or jurisdiction, a continuation or divisional patent application in such country or jurisdiction designed in good faith to preserve the status quo and to maintain full rights of further prosecution, in each case to the maximum extent possible under the circumstances. "**Patent-Related Matter**" means each of the following matters: (i) whether any new or useful process, composition of matter, formulation, design, device, kit or method of use or manufacture is reasonably expected to be patentable under Applicable Laws; (ii) inventorship of Program Inventions and, as a result, whether any particular Program Invention is a Targacept Program Invention, AstraZeneca Program Invention or Joint Program Invention; (iii) whether any Program Invention is a Product Invention; (iv) whether any action or decision with respect to the Prosecution and Maintenance of any Consensus Patent Rights, including any action contemplated by clause (v) below, would be contrary to the best interests of the Development and Commercialization of the Lead Compound or Licensed Products that are comprised of or contain the Lead Compound on a global basis; and (v) with respect to Patent Rights that claim or cover any Program Invention, whether it is reasonably practicable to separate into discrete applications (i) claims that solely claim the composition of matter, a method of use or Manufacture of or a pharmaceutical preparation containing or comprising (including the pharmaceutical composition of), or solely cover the research, development, Manufacture, use, import, offer to sell or sale of, any Compound or Licensed Product and (ii) claims other than as specified in the foregoing clause (i) (each of the Patent-Related Matters in clauses (iv) and (v), a "**Consensus Patent-Related Matter**").

7.5.2 *Dispute Resolution*. In case of a dispute between the Patent Coordinators over any Patent-Related Matter that is not determined or resolved as of the Patent-Related Matter Resolution Deadline for such Patent-Related Matter, such dispute shall be resolved by patent counsel who (and whose firm) is mutually acceptable to both Parties, acting reasonably. In the event the Parties are unable to select mutually acceptable patent counsel within ******** Business Days after either Party requests such selection in writing, then each Party shall select a patent counsel and the two (2) Party-selected patent counsels shall mutually select a third patent counsel to resolve such dispute within ******** Business Days after expiration of such first ******** Business Day period. Each Party shall, within ******** Business Days after the selection of patent counsel to determine or resolve such Patent-Related Matter, propose in writing a determination or resolution of such Patent-Related Matter. Such patent counsel shall be directed to determine or resolve such Patent-Related Matter not later than ******** Business Days after receipt of such written proposals, such determination or resolution to be final and binding between the Parties; provided that, in the case of a Patent-Related Matter described in clause (iv) of Section 7.5.1, such patent counsel must select the determination or resolution proposed by one of the Parties that more closely reflects the best interests of the Development and Commercialization of the Lead Compound and Licensed Products that are comprised of or contain the Lead Compound on a global basis. Both Parties shall cooperate in all reasonable respects with such patent counsel's reasonable requests for assistance and information in connection with its determination hereunder. Expenses of such patent counsel shall be shared equally by the Parties.

7.6 **Employees and Agents**. Each Party shall obtain from each of its Affiliates, Sublicensees, employees and agents, and from the employees and agents of its Affiliates, who are engaged in research or Development activities conducted pursuant to this Agreement or who otherwise have access to the other Party's Confidential Information, such undertakings and agreements as are necessary to ensure that each Party shall, by virtue of this Agreement, receive from the other Party, without payments beyond those required by Article 5, Section 11.5.1(f) or Section 11.5.3(i), the licenses and other rights granted to the other Party hereunder.

7.7 **Prosecution and Maintenance**.

7.7.1 *Prosecution and Maintenance*.

(a) AstraZeneca. Subject to Section 7.7.2(a) and Section 7.7.2(b), as between the Parties, AstraZeneca, acting through patent counsel or agents of its choice, shall be responsible for Prosecution and Maintenance of all Targacept Patent Rights, Targacept Program Patent Rights that solely claim the composition of matter, a method of use or Manufacture of or a pharmaceutical preparation containing or comprising (including the pharmaceutical composition of), or solely cover the research, development, Manufacture, use, import, offer to sell or sale of, any Compound or Licensed Product, AstraZeneca Patent Rights, AstraZeneca Program Patent Rights and Joint Program Patent Rights. The Patent Costs incurred by AstraZeneca in connection with Prosecution and Maintenance of Patent Rights contemplated by this Section 7.7.1(a) shall be the sole responsibility of AstraZeneca and, for clarity, shall not be Development Costs.

(b) Targacept. Subject to Section 7.7.2(b), Targacept, acting through patent counsel or agents of its choice, shall have the sole right and responsibility for Prosecution and Maintenance of all Targacept Program Patent Rights not described in Section 7.7.1(a). The Patent Costs incurred by Targacept in connection with Prosecution and Maintenance of such Targacept Program Patent Rights shall be the sole responsibility of Targacept and, for clarity, shall not be Development Costs.

(c) ******** Application. As soon as practicable after the Effective Date, Targacept and AstraZeneca shall take such actions as are necessary to generate discrete applications from the ******** Application, whether by filing divisionals, continuations, continuations-in-part or otherwise, so as to separate in a discrete application(s) the claims that solely claim a method of use of, or solely cover the research, development, Manufacture, use, import, offer to sell or sale of, one or more Compounds or Licensed Products. It is expressly acknowledged and agreed that, notwithstanding any other provision of this Agreement: (i) beginning at the time of such action, only the application(s) generated from the ******** Application in accordance with this Section 7.7.1(c) that solely claims a method of use of, or solely covers the research, development, Manufacture, use, import, offer to sell or sale of, any Compound or Licensed Product shall be deemed included within the Targacept Patent Rights; and (ii) no other application generated from the ******** Application in accordance with this Section 7.7.1(c) shall be deemed included within the Targacept Patent Rights or Targacept Program Patent Rights or otherwise subject to this Agreement.

(d) Program Patent Rights. Whenever reasonably practicable without being contrary to the best interests of the Development and Commercialization of the Lead Compound or Licensed Products that are comprised of or contain the Lead Compound on a global basis, Targacept and AstraZeneca shall take such actions as are necessary with respect to Patent Rights that claim or cover any Program Invention so as to separate into discrete patent application(s) (i) claims that solely claim the composition of matter, a method of use or Manufacture of or a pharmaceutical preparation containing or comprising (including the pharmaceutical composition of), or solely cover the research, development, Manufacture, use, import, offer to sell or sale of, one or more Compounds or Licensed Products and (ii) claims other than as specified in the foregoing clause (i).

7.7.2 *Consensus; Cooperation*.

(a) Prosecution and Maintenance of Consensus Patent Rights. Notwithstanding Section 7.7.1(a) or any other provision of this Agreement, it is the intent of the Parties that all decisions in the Prosecution and Maintenance of (i) Targacept Patent Rights (including the Existing Patent Rights), (ii) Targacept Program Patent Rights that solely claim the ******** or a ******** or ******** or a ******** or ******** (including ********), or solely cover the research, development, Manufacture, use, import, offer to sell or sale of, one or more Compounds or Licensed Products, and (iii) Joint Program Patent Rights (collectively (clauses (i), (ii) and (iii), "**Consensus Patent Rights**") be made by the consensus of AstraZeneca and Targacept acting through their respective Patent Coordinators (and, in the case of a Patent Coordinator who is not a patent counsel, in consultation with patent counsel); provided that, with respect to each patent or patent application within Consensus Patent Rights: (A) for each Prosecution and Maintenance action or decision with respect thereto, if the Parties' respective Patent Coordinators have undertaken diligent efforts in good faith to reach consensus but are unable to do so by the applicable Patent-Related Matter Deadline, AstraZeneca shall, subject to clause (B) below and except as otherwise provided in clause (C) below, have the right to take such action or make such decision; (B) in no event shall AstraZeneca take any action or make any decision with respect to the Prosecution and Maintenance thereof that would be contrary to the best interests of the Development and Commercialization of the Lead Compound and Licensed Products that are comprised of or contain the Lead Compound on a global basis without Targacept's prior written consent; and (C) notwithstanding clause (A) above, any action or decision with respect thereto that is the subject of a Consensus Patent-Related Matter shall be resolved in accordance with Section 7.5 and AstraZeneca shall proceed only in accordance with such resolution.

(b) Cooperation.

(i) At either Party's request, the other Party shall cooperate with and assist the requesting Party in all reasonable respects at the requesting Party's expense, in connection with the requesting Party's Prosecution and Maintenance of Patent Rights in accordance with Section 7.7.1(a) or Section 7.7.1(b), as the case may be.

(ii) In addition, without limitation of Section 7.7.2(a): AstraZeneca shall: (A) regularly provide Targacept with copies of all patent applications (including drafts) to be filed hereunder that are within the Consensus Patent Rights and other material submissions and correspondence with all patent offices with respect to Consensus Patent Rights, in sufficient time to allow for review and comment by Targacept; (B) provide Targacept and its patent counsel with an opportunity to consult with AstraZeneca and its patent counsel regarding the filing and contents of any such application, amendment, submission or response; (C) take into consideration in good faith the advice and suggestions of Targacept and its patent counsel; and (D) subject to Section 7.7.4(a), pursue in good faith all reasonable claims requested by Targacept in the Prosecution and Maintenance of Consensus Patent Rights.

(iii) In addition, Targacept shall: (A) regularly provide AstraZeneca with copies of all patent applications (including drafts) to be filed hereunder that both (1) are within the Targacept Program Patent Rights and (2) claim the ******** or a ******** or ******** or a ******** or ******** (including the ********), or cover the research, development, Manufacture, use, import, offer to sell or sale of, Compounds and Licensed Products, but are not Consensus Targacept Program Patent Rights (such patent applications, together with all Patent Rights with respect thereto, "**Non-Consensus Targacept Program Patent Rights**") and other material submissions and correspondence with all patent offices with respect to Non-Consensus Targacept Program Patent Rights, in sufficient time to allow for review and comment by AstraZeneca; (B) provide AstraZeneca and its patent counsel with an opportunity to consult with Targacept and its patent counsel regarding the filing and contents of any such application, amendment, submission or response; (C) take into consideration in good faith the advice and suggestions of AstraZeneca and its patent counsel; and (D) subject to Section 7.7.4(b), pursue in good faith all reasonable claims requested by AstraZeneca in the Prosecution and Maintenance of Non-Consensus Targacept Program Patent Rights.

7.7.3 *Disclosure*. Each Party shall promptly notify the other Party, through its Patent Coordinator, of any Program Invention and discuss with the other Party, through its Patent Coordinator, the filing of any patent application with respect thereto.

7.7.4 *Abandonment.*

(a) If AstraZeneca decides to abandon or to allow to lapse any Consensus Patent Rights, or any Patent Rights that it knows are AstraZeneca Patent Rights, in any country or jurisdiction in the world, AstraZeneca shall inform Targacept of such decision promptly and, in any event, so as to provide Targacept a reasonable amount of time to meet any applicable deadline to establish or preserve such Consensus Patent Rights or AstraZeneca Patent Rights in such country or jurisdiction; provided that, in such event, solely with respect to Consensus Patent Rights, the licenses granted by Targacept pursuant to Section 4.1.1 shall thereupon exclude such abandoned Consensus Patent Rights. Targacept shall have the right to assume responsibility for continuing Prosecution and Maintenance of such Patent Rights in such country or jurisdiction and paying any required fees to Prosecute and Maintain such Patent Rights in such country or jurisdiction, all at Targacept's sole expense, through patent counsel or agents of its choice. Upon transfer of AstraZeneca's responsibility for Prosecution and Maintenance of any Patent Rights to Targacept under this Section 7.7.4(a), AstraZeneca shall promptly deliver to Targacept copies of all necessary files related to the Patent Rights with respect to which responsibility has been transferred and shall take all actions and execute all documents reasonably necessary for Targacept to assume such Prosecution and Maintenance.

(b) If Targacept decides to abandon or to allow to lapse any Patent Rights that it knows to be Non-Consensus Targacept Program Patent Rights in any country or jurisdiction in the Territory, Targacept shall inform AstraZeneca of such decision promptly and, in any event, so as to provide AstraZeneca a reasonable amount of time to meet any applicable deadline to establish or preserve such Non-Consensus Targacept Program Patent Rights in such country or jurisdiction. AstraZeneca shall have the right to assume responsibility for continuing Prosecution and Maintenance of such Non-Consensus Targacept Program Patent Rights in such country or jurisdiction and paying any required fees to Prosecute and Maintain such Non-Consensus Targacept Program Patent Rights in such country or jurisdiction, all at AstraZeneca's sole expense, through patent counsel or agents of its choice. Upon transfer of Targacept's responsibility for Prosecution and Maintenance of any Non-Consensus Targacept Program Patent Rights to AstraZeneca under this Section 7.7.4(b), Targacept shall promptly deliver to AstraZeneca copies of all necessary files related to the Non-Consensus Targacept Program Patent Rights with respect to which responsibility has been transferred and shall take all actions and execute all documents reasonably necessary for AstraZeneca to assume such Prosecution and Maintenance.

7.7.5 *Alignment of Interests*. The Parties acknowledge that as of the Execution Date it is not possible to identify and agree on all of the actions or decisions in the Prosecution and Maintenance of Consensus Patent Rights that would be contrary to the best interests of the Development and Commercialization of the Lead Compound or Licensed Products that are comprised of or contain the Lead Compound on a global basis. However, solely for purposes of this Article 7, the Parties agree that, without limitation, each of the following actions or decisions in the Prosecution and Maintenance of Consensus Patent Rights would be contrary to the best interests of the Development and Commercialization of the Lead Compound and Licensed Products that contain the Lead Compound on a global basis: (a) any action or decision that would ******** of such Consensus Patent Rights, unless all of (i) such action or decision would result in subject matter that is or would be ******** in a particular patent application being ********, (ii) a continuation or divisional patent application to ******** all such ******** subject matter is permitted under applicable patent laws, regulations or administrative process to be filed in the applicable country or jurisdiction in a manner that preserves full rights of further prosecution and (iii) a continuation or divisional patent application to ******** all such ******** subject matter is filed by AstraZeneca by all applicable deadlines and otherwise diligently Prosecuted and Maintained by AstraZeneca; (b) any action or decision that would ******** such Patent Rights; (c) ******** that is required under applicable patent laws, regulations or administrative process to be ******** any patent office or examiner; (d) ********; and (e) ******** a ******** or ******** as ******** is known not to be ********.

7.7.6 *Targacept Sublicense Agreements*. Notwithstanding anything in this Agreement to the contrary, it is understood and agreed that the respective rights and obligations of the Parties pursuant to this Section 7.7 are subject in all respects to the rights of USFRF under the USFRF Agreement and the rights of Yale under the Yale Agreement. AstraZeneca agrees that, consistent with Section 6.1 of the USFRF Agreement, it shall exercise its rights and perform its obligations with respect to the Prosecution and Maintenance of any Patent Rights licensed by USFRF to Targacept pursuant to the USFRF Agreement and sublicensed to AstraZeneca hereunder in good faith and it shall give due consideration in good faith to comments timely received from USFRF or its patent counsel, through Targacept, with respect to the Prosecution and Maintenance of such Patent Rights. AstraZeneca acknowledges and agrees that USFRF shall be a third party beneficiary solely with respect to this Section 7.7.6; provided that USFRF shall enforce its rights as a third party beneficiary solely pursuant to and in accordance with Section 12.1, *mutatis mutandis*.

7.8 **Patent Listings**. AstraZeneca shall have the sole right to make all filings with the Regulatory Authorities with respect to the Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights and AstraZeneca Program Patent Rights, including as required or allowed in connection with: (a) in the U.S. Territory, the Orange Book and (b) in the ROW Territory, under the national implementations of Article 10.1(a)(iii) of Directive 2001/EC/83 or other international equivalents. Targacept shall, if requested by AstraZeneca and at AstraZeneca's reasonable expense: (i) provide to AstraZeneca all Information in Targacept's possession, including a correct and complete list of Consensus Patent Rights and Non-Consensus Targacept Program Patent Rights, covering any Compound or Licensed Product or otherwise necessary or reasonably useful to enable AstraZeneca to make such filings with Regulatory Authorities with respect to Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights and AstraZeneca Program Patent Rights; and (ii) cooperate in all reasonable respects with AstraZeneca's reasonable requests in connection therewith, including meeting any submission deadlines, in each case to the extent required or permitted by Applicable Laws. AstraZeneca shall, to the extent reasonably practicable, notify Targacept in writing of each such filing with a Regulatory Authority with respect to any Consensus Patent Rights or Non-Consensus Targacept Program Patent Rights.

7.9 ********. AstraZeneca shall have the ******** right to ******** in the Territory regarding ******** for Licensed Products, including (a) in the U.S. Territory with respect to ********, (b) in the ROW Territory pursuant to ******** and (c) in the Territory with respect to any other ******** that are now or become available in the future; provided that, with respect to ********, neither the effect of ******** on a ******** hereunder nor the effect of ******** on sales, profit or market share of any product (other than a Licensed Product) marketed or sold by AstraZeneca or any of its Affiliates shall be ********. Upon request by AstraZeneca, Targacept shall cooperate in all reasonable respects in the implementation of AstraZeneca's decisions under this Section 7.9.

7.10 **Liability**.

7.10.1 *AstraZeneca*. To the extent that AstraZeneca is Prosecuting and Maintaining Consensus Patent Rights, AstraZeneca Patent Rights or AstraZeneca Program Patent Rights (or any other Patent Rights with respect to the Collaboration that the Parties expressly agree are to be Prosecuted and Maintained by AstraZeneca) or otherwise exercising its rights under Sections 7.7 through 7.9, if AstraZeneca has complied with Sections 7.7 through 7.9 (including Section 7.7.2(a) and the proviso in Section 7.9) and the Targacept Sublicense Agreements, neither AstraZeneca nor any of its employees, agents or representatives shall be liable to Targacept in respect of any act, omission, default or neglect taken or omitted in good faith by any such employee, agent or representative in connection with such activities.

7.10.2 *Targacept*. To the extent that Targacept is Prosecuting and Maintaining Non-Consensus Targacept Program Patent Rights (or any Patent Rights with respect to the Collaboration that the Parties expressly agree are to be Prosecuted and Maintained by Targacept) or otherwise exercising its rights under Section 7.7, if Targacept has complied with Section 7.7, neither Targacept nor any of its employees, agents or representatives shall be liable to AstraZeneca in respect of any act, omission, default or neglect taken or omitted in good faith by any such employee, agent or representative in connection with such activities.

7.11 **CREATE Act**. Notwithstanding anything to the contrary in Sections 7.1 through 7.9, neither Party shall have the right to make an election under the Cooperative Research and Technology Enhancement Act of 2004, 35 U.S.C. 103(c)(2)-(c)(3) (the "**CREATE Act**") when exercising its rights under Sections 7.1 through 7.9 without the prior written consent of the other Party. With respect to any such permitted election, the Parties shall use diligent efforts to cooperate and coordinate their activities with respect to any submissions, filings or other activities in support thereof. The Parties acknowledge and agree that this Agreement is a "joint research agreement" as defined in the CREATE Act.

7.12 **Legal Actions**.

7.12.1 *Third Party Infringement*.

(a) Notice. In the event either Party becomes aware of (i) any suspected infringement of any Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights or AstraZeneca Program Patent Rights or (ii) any certification filed under the Hatch-Waxman Act claiming that any Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights or AstraZeneca Program Patent Rights are invalid or unenforceable or claiming that any Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights or AstraZeneca Program Patent Rights will not be infringed by the making, use, offer for sale, sale or import of a product for which an application under the Hatch-Waxman Act is filed, or any equivalent or similar certification or notice in any other jurisdiction in the Territory (each of clauses (i) and (ii), an "**Infringement**"), in each case (clauses (i) and (ii)) such Party shall promptly notify the other Party and provide it with all details of such Infringement of which it is aware (each, an "**Infringement Notice**"); provided that each Party shall give the other Party an Infringement Notice not later than ******** Business Days after it becomes aware of any Infringement described in clause (ii) above.

(b) AstraZeneca Right to Prosecute Infringement. As between the Parties, AstraZeneca shall have the first right, but not the obligation, in the Major Countries, and sole right, but not the obligation, in any other countries in the Territory, to prosecute an Infringement by taking commercially reasonable steps; provided that, with respect to prosecuting any Infringement of any Non-Consensus Targacept Program Patent Rights, without limitation of Section 7.12.1(f), AstraZeneca shall collaborate closely with Targacept with respect to prosecuting such Infringement and consider in good faith, and not unreasonably reject or act contrary to, Targacept's advice and suggestions with respect thereto taking into account Targacept's interests under such Non-Consensus Targacept Program Patent Rights that are not related to Compounds or Licensed Products. All costs, including attorneys' fees, relating to such legal proceedings or other action shall be borne by AstraZeneca, subject to Section 7.12.1(g).

(c) Targacept Right to Prosecute Infringement in Major Countries. If AstraZeneca does not take or initiate commercially reasonable steps to prosecute an Infringement that occurs in a Major Country within ******** days after receipt or delivery of any Infringement Notice (or ******** days in the case of an Infringement described in Section 7.12.1(a)(ii)), then AstraZeneca shall notify Targacept within ******** after the end of such period and, as between the Parties, Targacept shall have the right, but not the obligation, to do so upon written notice to AstraZeneca and shall bear all costs to do so, subject to Section 7.12.1(g); provided that if AstraZeneca has commenced good faith negotiations with an alleged infringer for elimination of such Infringement within such ******** day (or, if applicable, ******** day) period, AstraZeneca shall have an additional ******** days (or an additional ******** days in the case of an Infringement described in Section 7.12.1(a)(ii)) to conclude its negotiations before Targacept may take steps to prosecute such Infringement.

(d) Settlement. The Party prosecuting any Infringement proceedings or other action under Section 7.12.1(b) or Section 7.12.1(c) shall have the right to settle or otherwise dispose of such Infringement proceedings or other action on such terms as such Party shall determine in its sole discretion, including, with respect to Infringement proceedings or other actions for which AstraZeneca is the prosecuting Party, by granting a license or sublicense to a Third Party under any rights granted to AstraZeneca under Section 4.1.1; provided that, notwithstanding the foregoing, (i) no such settlement or other disposition shall impose any restriction or obligation on or admit fault of the other Party and (ii) where AstraZeneca is prosecuting any Infringement proceeding with respect to Non-Consensus Targacept Program Patent Rights, no such settlement or other disposition shall concede, directly or indirectly, the invalidity or enforceability of, or materially weaken or reduce the scope of, such Non-Consensus Targacept Program Patent Rights.

(e) Right to Representation. Each Party shall have the right, at its sole expense, to participate and be represented by counsel that it selects, in any legal proceedings or other action instituted under Section 7.12.1(b) or Section 7.12.1(c) by the other Party. If a Party with the right to initiate legal proceedings under this Section 7.12.1 to eliminate an Infringement lacks standing to do so and the other Party has standing to initiate such legal proceedings, then the Party with the right to initiate legal proceedings under Section 7.12.1 may name the other Party as plaintiff in such legal proceedings or may require the Party with standing to initiate such legal proceedings at the expense of the other Party (subject to Section 7.12.1(g)).

(f) Cooperation. In any legal proceedings or other action instituted under this Section 7.12.1, the Parties shall cooperate with and assist each other in all reasonable respects. Upon the reasonable request of the Party instituting such action, suit or proceeding, the other Party shall join such legal proceedings or other action and shall be represented using counsel of its own choice, at the requesting Party's expense.

(g) Allocation of Proceeds. Any amounts recovered by either Party pursuant to actions under Section 7.12.1(b) or Section 7.12.1(c) with respect to any Infringement in the Territory, whether by settlement or judgment, shall be allocated in the following order: (i) first, to reimburse AstraZeneca and Targacept for their reasonable ******** expenses in making such recovery (which amounts shall be allocated pro rata if insufficient to cover the totality of such expenses); and (ii) then (A) if Targacept took steps to eliminate the Infringement pursuant to Section 7.12.1(c) (or to defend any action or claim pursuant to Section 7.12.2), any remainder to Targacept or (B) otherwise, any remainder to AstraZeneca and Targacept in the same ratio as (1) ******** percent (********%) of AstraZeneca's historic profits on Net Sales of Licensed Products in the ROW Territory (if such Infringement occurred in any country in the ROW Territory) or ******** percent (********%) of AstraZeneca's historic profits on Net Sales of Licensed Products in the U.S. Territory (if such Infringement occurred in the U.S. Territory), bears to (2) the historic royalties paid to Targacept under Section 5.3.1(a) (if such Infringement occurred in any country in the ROW Territory) or the historic royalties paid to Targacept under Section 5.3.1(b) (if such Infringement occurred in the U.S. Territory), as the case may be, as determined by AstraZeneca consistently, reasonably and in good faith.

7.12.2 *Invalidity or Unenforceability Defenses or Actions*. In the event that a Third Party or Sublicensee asserts as a defense or as a counterclaim in any Infringement action under Section 7.12.1 that any Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights or AstraZeneca Program Patent Rights are invalid or unenforceable, then the Party pursuing such Infringement action shall promptly give written notice to the other Party. As between the Parties, AstraZeneca shall have the first right, but not the obligation, through counsel of its choice and at its sole expense (subject to the last sentence of this Section 7.12.2), to respond to and control such defense or defend against such counterclaim (as applicable), including the right to settle or otherwise compromise such claim at its sole expense; provided that: (a) notwithstanding the foregoing, no such settlement or other compromise shall impose any restriction or obligation on or admit fault of Targacept or concede, directly or indirectly, the invalidity or enforceability of, or materially ******** or ******** the ******** of, any Non-Consensus Targacept Program Patent Rights; and (b) with respect to any claim of invalidity or unenforceability of any Non-Consensus Targacept Program Patent Rights, AstraZeneca shall collaborate closely with Targacept with respect to the defense of such claim and consider in good faith, and not unreasonably reject or act contrary to, Targacept's advice and suggestions with respect thereto taking into account Targacept's interests under such Non-Consensus Targacept Program Patent Rights that are not related to Compounds or Licensed Products. If AstraZeneca notifies Targacept in writing that it does not wish to respond to such defense or defend against, or settle or otherwise compromise, such counterclaim (as applicable), Targacept shall have the right, but not the obligation, through counsel of its choice and at its sole expense (subject to the last sentence of this Section 7.12.2), upon written notice to AstraZeneca, to respond to such defense or defend against such counterclaim (as applicable); provided that Targacept shall use diligent efforts to provide written notice to AstraZeneca sufficiently in advance of ceasing to defend or prosecute such defense or counterclaim so as to enable AstraZeneca to assume control of such defense or counterclaim if it so elects and shall obtain the written consent of AstraZeneca (not to be unreasonably withheld, conditioned or delayed and, absent compelling reasons affecting both Parties in substantially the same manner, not to be withheld, conditioned or delayed unless AstraZeneca provides evidence satisfactory to Targacept, acting reasonably, that such settlement or compromise is not in the best interests of the Development and Commercialization, globally, of the Lead Compound and Licensed Products that are comprised of or contain the Lead Compound), prior to settling or otherwise compromising such defense or counterclaim. Further, if a Third Party asserts, in a declaratory judgment action or similar action or claim filed by such Third Party, that any Consensus Patent Rights, Non-Consensus Targacept Program Patent Rights, AstraZeneca Patent Rights or AstraZeneca Program Patent Rights are invalid or unenforceable, then the Party first becoming aware of such action or claim shall promptly give written notice to the other Party. As between the Parties, AstraZeneca shall have the first right, but not the obligation, through counsel of its choice, and at its sole expense (subject to the last sentence of this Section 7.12.2), to defend against such action or claim, including the right to settle or otherwise compromise such claim; provided that: (i) notwithstanding the foregoing, no such settlement or other compromise shall impose any restriction or obligation on or admit fault of Targacept or concede, directly or indirectly, the invalidity or enforceability of, or materially ******** or ******** the ******** of, any Non-Consensus Targacept Program Patent Rights; and (ii) with respect to any action or claim asserting the invalidity or unenforceability of any Non-Consensus Targacept Program Patent Rights, AstraZeneca shall collaborate closely with Targacept with respect to the defense of such action or claim and consider in good faith Targacept's advice and suggestions, and not unreasonably reject or act contrary to, with respect thereto taking into account Targacept's interests under such Non-Consensus Targacept Program Patent Rights that are not related to Compounds or Licensed Products. If AstraZeneca notifies Targacept in writing that it does not wish to respond to or defend against or settle or otherwise compromise such action or claim, Targacept shall have the right, but not the obligation, through counsel of its choice and at its sole expense (subject to the last sentence of this Section 7.12.2), upon written notice to AstraZeneca, to defend against and control such action or claim; provided that Targacept shall use diligent efforts to provide written notice to AstraZeneca sufficiently in advance of ceasing to defend such action or claim so as to enable AstraZeneca to assume control of such defense if it so elects and shall obtain the written consent of AstraZeneca (not to be unreasonably withheld, conditioned or delayed and, absent compelling reasons affecting both Parties in substantially the same manner, not to be withheld, conditioned or delayed unless AstraZeneca provides evidence satisfactory to Targacept, acting reasonably, that such settlement or compromise is not in the best interests of the Development and Commercialization, globally, of the Lead Compound and Licensed Products that are comprised of or contain the Lead Compound) prior to settling or otherwise compromising such action or claim. Any amounts recovered in connection with any action, claim or suit under this Section 7.12.2 shall be allocated between the Parties as provided in Section 7.12.1(g).

7.12.3 *Defense of Claims*. In the event that any action, suit or proceeding is brought against either Party or any Affiliate or Sublicensee of either Party alleging the infringement of Patent Rights or other intellectual property rights of a Third Party by reason of the Development or Commercialization, including the Manufacture, use or sale, of any Compound or Licensed Product, such Party shall notify the other Party within ******** Business Days of the earlier of (a) receipt of service of process in such action, suit or proceeding or (b) the date such Party becomes aware that such action, suit or proceeding has been instituted and provide the other Party with all the details of such action, suit or proceeding of which such Party is aware. As between the Parties, AstraZeneca shall have the first right, but not the obligation, to defend such action, suit or proceeding at its sole expense. If AstraZeneca notifies Targacept in writing that it does not wish to defend such action, suit or proceeding, Targacept shall have the right, but not the obligation, through counsel of its choice and at its sole expense, upon written notice to AstraZeneca, to defend such action, suit or proceeding; provided that Targacept shall use diligent efforts to provide written notice to AstraZeneca sufficiently in advance of ceasing to defend such action, suit or proceeding so as to enable AstraZeneca to assume control of such defense if it so elects. Each Party shall have the right, at its sole expense, to be represented by counsel that it selects, in any action, suit or proceeding defended by the other Party under this Section 7.12.3. In no event shall either Party settle or otherwise resolve any claims included in such action, suit or proceeding brought against the other Party or any of its Affiliates or Sublicensees without the prior written consent of the other Party, which shall not be unreasonably withheld, conditioned or delayed and, absent compelling reasons affecting both Parties in substantially the same manner, shall not be withheld, conditioned or delayed unless such other Party provides evidence satisfactory to such first Party, acting reasonably, that such settlement or other resolution is not in the best interests of the Development and Commercialization, globally, of the Lead Compound and Licensed Products that are comprised of or contain the Lead Compound). For clarity, either Party shall have the right to settle or otherwise resolve claims of infringement asserted against it, in its sole and absolute discretion.

7.12.4 *Cooperation*. Each Party (the "**Cooperating Party**") shall provide to the other Party (the "**Acting Party**") all assistance reasonably requested by the Acting Party in connection with any action, claim or suit under Section 7.12.1, 7.12.2 or 7.12.3, including allowing the Acting Party reasonable access during normal business hours to the Cooperating Party's files and documents and to the Cooperating Party's personnel who may have possession of relevant information. The Cooperating Party shall use diligent efforts (a) likewise to procure for the Acting Party reasonable access to former personnel of the Cooperating Party and (b) to cause any Third Parties owning Patent Rights licensed to the Cooperating Party, and any Third Parties that are licensees of any of the Cooperating Party's Patent Rights, to use diligent efforts to assist and cooperate with the Acting Party in connection with the response to such action, claim or suit under Section 7.12.1, 7.12.2 or 7.12.3. In addition to the foregoing, prior to the initiation of any action, claim or suit under Section 7.12.1, 7.12.2 or 7.12.3, upon the reasonable request of AstraZeneca, Targacept shall request USFRF and Yale to provide AstraZeneca access to relevant personnel to enable AstraZeneca to prepare for any such possible action, claim or suit.

7.12.5 *Third Party Licenses*. If in the reasonable opinion of AstraZeneca the Development or Commercialization of any Compound or Licensed Product by AstraZeneca, any of its Affiliates or any of its or their Sublicensees, Distributors or Net Sales Distributors infringes or misappropriates any Patent Rights, trade secret or other intellectual property right of a Third Party in any country in the Territory, such that AstraZeneca, any of its Affiliates or any of its or their Sublicensees, Distributors or Net Sales Distributors cannot Develop or Commercialize such Compound or Licensed Product in such country without infringing such Patent Rights, trade secret or other intellectual property right of such Third Party, then, as between the Parties, AstraZeneca shall have the first right, but not the obligation, through counsel of its choice and at its sole expense (subject to Section 5.3.1(c)(ii), if and to the extent applicable), and in its sole discretion, to negotiate and obtain a license from such Third Party as necessary for AstraZeneca and its Affiliates, Sublicensees, Distributors and Net Sales Distributors to Develop and Commercialize Compound and any Licensed Product in such country.

7.12.6 *Targacept Sublicense Agreements*. Notwithstanding anything in this Agreement to the contrary, it is understood and agreed that the respective rights and obligations of the Parties pursuant to this Section 7.12 are subject in all respects to the rights of USFRF under the USFRF Agreement and the rights of Yale under the Yale Agreement.

7.13 **Trademarks**.

7.13.1 *Amplixa Trademarks*. Targacept hereby assigns to AstraZeneca the Existing Trademarks and all rights and goodwill with respect thereto. Targacept shall duly execute and deliver, or cause to be duly executed and delivered, such instruments and shall do and cause to be done such acts and things, including the filing of such assignments, agreements, documents and instruments, as may be necessary to carry out, or as AstraZeneca may reasonably request in connection with, this Section 7.13.1. In jurisdictions where trademark laws may prohibit current assignment of the Existing Trademarks, the Parties will mutually agree on the best approach to ultimately assign the Existing Trademarks to AstraZeneca.

7.13.2 *Product Trademarks*. AstraZeneca shall have the sole right to select the Product Trademarks for the marketing and sale of Licensed Products in the Territory. AstraZeneca shall own such Product Trademarks and all rights and goodwill with respect thereto. AstraZeneca shall have the right, using legal counsel of its own choosing and at its sole expense, to file, maintain, defend, and enforce the Product Trademarks. Targacept shall not, and shall not permit its Affiliates to, use any Trademark that is the same as or confusingly similar to, or misleading or deceptive with respect to, the Product Trademarks.

7.14 **Product Information**. Subject to Sections 11.5.1 and 11.5.3, AstraZeneca shall have sole and exclusive ownership of all right, title and interest on a worldwide basis in and to any and all Product Information. Targacept agrees to assign, and hereby assigns, to AstraZeneca all right, title and interest that Targacept may acquire from time to time in any and all Product Information and shall, at AstraZeneca’s reasonable expense, execute all documents and do all proper actions reasonably required by AstraZeneca from time to time to perfect AstraZeneca’s title to and ownership thereof.

ARTICLE 8
CONFIDENTIALITY

8.1 **Targacept Licensed Product Information**. Targacept recognizes that by reason of, *inter alia*, AstraZeneca's status as an exclusive licensee pursuant to the grants under Section 4.1.1, AstraZeneca has an interest in Targacept's retention in confidence of certain information of Targacept. Accordingly, until the expiration of AstraZeneca's exclusive position with respect to the last Licensed Product under Section 4.1.1, Targacept shall, and shall cause its Affiliates and Sublicensees and its and their respective officers, directors, employees and agents to, keep confidential, and not publish or otherwise disclose, and not use for any purpose other than to perform its obligations, or exercise its rights, under this Agreement, the Co-Promotion Agreement, if any, or the Backup R&D Programs Agreement, if any, any Information owned or Controlled by, Targacept, to the extent relating to: (a) any Compound or Licensed Product or any Regulatory Documentation, including Product Regulatory Approvals, with respect thereto or (b) the Development or Commercialization of any Compound or Licensed Product (collectively, clauses (a) and (b), the "**Targacept Licensed Product Information**"); except to the extent (i) such Targacept Licensed Product Information was available to the public generally or otherwise part of the public domain at the time it was disclosed or made available to, or received or accessed by, AstraZeneca or became available to the public generally or otherwise part of the public domain after it was disclosed or made available to, or received or accessed by, AstraZeneca through no fault of Targacept, any of its Affiliates or any of its or their respective officers, directors, employees or agents, (ii) such disclosure or use is expressly permitted by Section 8.3 or (iii) such disclosure or use is otherwise expressly permitted by the terms of this Agreement. For purposes of Section 8.3, both AstraZeneca and Targacept shall be deemed to be the Disclosing Party with respect to Targacept Licensed Product Information under Section 8.3 and both Targacept and AstraZeneca shall be deemed to be the Receiving Party with respect thereto. For clarity, to the extent Targacept Licensed Product Information is received by AstraZeneca pursuant to this Agreement, such Targacept Licensed Product Information shall also constitute Confidential Information of Targacept with respect to the use and disclosure of such Confidential Information by AstraZeneca, subject to the other terms and conditions of this Article 8, but the disclosure or making available to, or receipt or access by, AstraZeneca of Targacept Licensed Product Information shall not cause such Targacept Licensed Product Information to cease to be subject to the provisions of this Section 8.1 with respect to the use and disclosure of such Confidential Information by Targacept. In the event this Agreement is terminated (A) pursuant to Article 11 in its entirety, this Section 8.1 shall have no continuing force or effect with respect to the use or disclosure of Targacept Licensed Product Information by Targacept and its Affiliates and licensees or (B) with respect to one or more Terminated Territories, this Section 8.1 shall have no continuing force or effect with respect to the use or disclosure of Targacept Licensed Product Information by Targacept and its Affiliates and licensees in or for any Terminated Territory; provided that, in each case (clauses (A) and (B)) the Targacept Licensed Product Information, to the extent disclosed by Targacept to AstraZeneca hereunder, shall continue to be Confidential Information of Targacept, subject to the terms of Sections 8.2 and 8.3.

8.2 **Confidentiality; Exceptions**.

8.2.1 *Confidential Information*. "**Confidential Information**" means any Information and materials, patentable or otherwise (including Proprietary Materials, trade secrets, know-how, Inventions or discoveries, formulae, methods, processes, techniques and information relating to a Party's past, present and future marketing, financial, and research and development activities of any product or potential product or useful technology of a Party and the pricing thereof), together with the specific royalty rates and individual milestone amounts set forth in this Agreement (which, for clarity, shall be Confidential Information of both Parties), in any form (written, oral, photographic, electronic, magnetic, or otherwise), that is disclosed or made available to a Party by or on behalf of the other Party, or otherwise received or accessed by such other Party, before (including under the Existing CDA), on or after the Effective Date pursuant to this Agreement, in connection with the transactions contemplated hereby or any discussions or negotiations with respect thereto or in the course of performing its obligations or exercising its rights under this Agreement. For purposes of this Section 8.2, AstraZeneca shall be deemed to be the Disclosing Party with respect to Product Information and Targacept shall be deemed to be the Receiving Party with respect thereto.

8.2.2 *Obligation of Confidentiality*. Except to the extent otherwise expressly provided in this Agreement (including Section 8.1) or otherwise agreed in writing, the Parties agree that, during the Term and for a period of ********** years thereafter, each Party (the "**Receiving Party**") shall, and shall cause its Affiliates and Sublicensees and its and their respective officers, directors, employees and agents to, keep confidential, and not publish or otherwise disclose or use for any purpose other than as provided for in this Agreement, the Co-Promotion Agreement, if any, or the Backup R&D Programs Agreement, if any, any Confidential Information provided to it by the other Party (the "**Disclosing Party**").

8.2.3 *Exceptions*. Notwithstanding the foregoing, the Receiving Party's obligations with respect to Confidential Information of the Disclosing Party pursuant to Section 8.2.2 (including (x) in the case of AstraZeneca obligations with respect to Targacept Licensed Product Information but excluding (y) in the case of Targacept, obligations with respect to Targacept Licensed Product Information, which shall be subject to Section 8.1) shall not apply with respect to any such information that:

(a) was in the lawful knowledge and possession of the Receiving Party prior to the time it was disclosed or made available to, or received or accessed by, the Receiving Party, or was otherwise developed independently by the Receiving Party without reference to or use of the Disclosing Party's Confidential Information, as evidenced by written records kept in the ordinary course of business by, or other documentary proof of, the Receiving Party;

(b) was available to the public generally or otherwise part of the public domain at the time it was disclosed or made available to, or received or accessed by, the Receiving Party;

(c) became available to the public generally or otherwise part of the public domain after it was disclosed or made available to, or received or accessed by, the Receiving Party other than through any act or omission of the Receiving Party; or

(d) was disclosed to the Receiving Party, other than under an obligation of confidentiality to or at the direction of the Disclosing Party, by a Third Party who had no obligation to the Disclosing Party not to disclose such information.

8.3 **Authorized Disclosure**. Notwithstanding anything contained in Sections 8.1 and 8.2, (a) Targacept may disclose (i) Targacept Licensed Product Information and (ii) Confidential Information of AstraZeneca and (b) AstraZeneca may disclose Confidential Information of Targacept (including Targacept Licensed Product Information):

(A) to any employee or consultant of the Receiving Party or any of its Affiliates to enable the Receiving Party to exercise its rights or to carry out its responsibilities under this Agreement; provided that any such disclosure or transfer shall only be made to Persons who are bound by written obligations substantially as restrictive as those contained in Section 8.2.2;

(B)(1) on a need-to-know basis to the Receiving Party's legal and financial advisors; (2) as necessary or reasonably useful in connection with an actual or potential (x) permitted sublicense or assignment of the Receiving Party's rights hereunder or other permissible license of intellectual property rights, (y) debt or equity financing of the Receiving Party or (z) Change of Control involving the Receiving Party; provided that any disclosure pursuant to this clause (z) shall be limited to the terms of this Agreement (including providing a copy of this Agreement), as may be amended; and (3) to any Third Party to enable the Receiving Party to exercise its rights and perform its obligations under this Agreement (including, with respect to Targacept, its rights with respect to the Development and Commercialization of Compounds and Licensed Products with respect to any Terminated Territory); if, in the case of clauses (1) (except with respect to disclosures to the Receiving Party's legal advisors), (2) and (3) the receiving Person is bound by written obligations substantially as restrictive as those contained in Section 8.2.2;

(C) to the extent that such disclosure is necessary or reasonably useful for the Receiving Party to file, Prosecute and Maintain Patent Rights, or to file, prosecute or defend litigation against Third Parties related to Patent Rights, in accordance with this Agreement; provided that reasonable measures shall be taken to assure confidential treatment of such information, to the extent such protection is available;

(D) to the extent that such disclosure is required by Applicable Laws; provided that, in the case of any disclosure under this clause (D), the Receiving Party shall (1) unless not practicable under the circumstances, provide the Disclosing Party with reasonable advance notice of and an opportunity to comment on such disclosure, (2) if requested by the Disclosing Party, cooperate in all reasonable respects with the Disclosing Party's efforts to obtain confidential treatment or a protective order with respect to such disclosure, at the Disclosing Party's reasonable expense and (3) use diligent efforts in good faith to incorporate the comments of the Disclosing Party in such disclosure or request for confidential treatment;

(E) to the extent that such disclosure is made in response to a valid order of a court of competent jurisdiction or other competent authority; provided that: (1) the Receiving Party shall first have given notice to the Disclosing Party and, unless not practicable under the circumstances, given the Disclosing Party a reasonable opportunity to quash any such order or obtain a protective order requiring that such Targacept Licensed Product Information or Confidential Information, as applicable, that is the subject of such order be held in confidence by such court or authority or, if disclosed, be used only for the purpose for which the order was issued; and (2) if such order is not quashed or a protective order is not obtained, the Targacept Licensed Product Information or Confidential Information, as applicable, disclosed in response to such court or governmental order shall be limited to that information that is legally required to be disclosed in response to such court or governmental order;

(F) to the extent, without intending to expand the rights and obligations of Targacept with respect to regulatory matters hereunder, that such disclosure is made by AstraZeneca, Targacept or any of their respective Affiliates or Sublicensees (or licensees) to a Regulatory Authority as may be necessary or reasonably useful in connection with any filing, application or request for a Product Regulatory Approval; provided that reasonable measures shall be taken to assure confidential treatment of such information, to the extent such protection is available; or

(G) made by AstraZeneca or Targacept or their respective Affiliates or Sublicensees to permitted subcontractors, as may be necessary or reasonably useful in connection with the Development and Commercialization of any Compound or Licensed Product as contemplated by this Agreement; provided that such disclosures are made under obligations of confidentiality and non-use at least as protective as this Article 8.

8.4 **Press Release; Disclosure of Agreement**. On or promptly after the Execution Date, the Parties shall individually or jointly issue a public announcement of the execution of this Agreement in a form agreed upon by the Parties, and either Party may make subsequent public disclosure of the contents of such press release without further approval of the other Party. After issuance of such press release, except as required by Applicable Laws (including, for clarity, those relating to disclosure of material information to investors), neither Party shall issue any other press release or similar public announcement regarding the Development or Commercialization of Compounds or Licensed Products (it being understood that publication in scientific journals, presentation at scientific conferences and meetings and the like are intended to be covered by Section 8.5 and not subject to this Section 8.4), except with the other Party's consent or as permitted pursuant to Section 8.3; provided that, notwithstanding the foregoing, Targacept shall not require the consent of AstraZeneca for any press release or similar public announcement (but shall provide any such release to AstraZeneca for its review and consider any comments timely received in good faith) for the achievement of any Milestone Event or the payment of any milestone payment. The Parties agree to consult with each other reasonably and in good faith with respect to the text and timing of any such press release prior to the issuance thereof, and neither Party shall unreasonably withhold, condition or delay consent to any press release proposed for issuance by the other Party. Notwithstanding the foregoing, to the extent information regarding this Agreement has been publicly disclosed (or disclosed in a scientific or other conference), either Party may subsequently disclose the same information without the consent of the other Party. Each Party shall give the other Party a reasonable opportunity to review prior to submission (a) the first filing with the United States Securities and Exchange Commission describing the terms of this Agreement and (b) any subsequent filing that includes material terms of this Agreement disclosed for the first time and shall give due consideration to any reasonable comments by the non-filing Party relating to such filing, including the provisions of this Agreement for which confidential treatment should be sought.

8.5 **Publications**.

8.5.1 *First Approval*. The Parties acknowledge that scientific and medical publications and presentations of the activities hereunder will be made in a manner consistent with Targacept Sublicense Agreements or other agreements with Third Parties as in effect as of the Effective Date and applicable industry standards, but must be strictly monitored to prevent any premature publication or dissemination of results. Each Party agrees that it shall not: (a) publish or present, or permit to be published or presented, the results of the Development Program or the results of any Phase 4 Clinical Studies of any Licensed Product; or (b) register any Clinical Study to be conducted with respect to any Compound or Licensed Product at www.clinicaltrials.gov or any similar publicly-available registry with respect to clinical trials, in each case (clauses (a) and (b)) without the prior review by and approval of the other Party (not to be unreasonably withheld, conditioned or delayed and not to be withheld to the extent required by Applicable Laws). Each Party shall provide the other Party with the opportunity to review each of the submitting Party's proposed abstracts, manuscripts or presentations (including information to be presented verbally) with respect to the foregoing at least ******** days prior to its intended presentation or submission for publication, and such submitting Party agrees, upon written request from the other Party given within such ******** day period, not to submit such abstract or manuscript for publication or to make such presentation until the other Party is given up to ******** days from the date of such written request to seek appropriate patent protection for any material in such publication or presentation that it reasonably believes may be patentable.

8.5.2 *Prior Approved Publications*. Notwithstanding Section 8.5.1, once an abstract, manuscript or presentation has been reviewed and approved by a Party, the same content included in such abstract, manuscript or presentation does not have to be provided again to such Party for review for a later submission for publication.

8.5.3 *General*. In any permitted publication or presentation by a Party, the other Party's contribution shall be duly recognized, and co-authorship shall be determined in accordance with the standards established by the International Committee of Medical Journal Editors or such other standard prevailing at the time of such publication or presentation. Furthermore, with respect to any proposed abstracts, manuscripts or summaries of presentations by investigators or other Third Parties having the right to do so, such materials shall be subject to review under this Section 8.5 to the extent that AstraZeneca or Targacept (as the case may be) has the right to do so.

ARTICLE 9
REPRESENTATIONS AND WARRANTIES

9.1 **Mutual Representations and Warranties**. Targacept and AstraZeneca each represents and warrants to the other, as of the Execution Date, as follows:

9.1.1 *Organization*. It is a corporation duly organized, validly existing and in good standing under the laws of the jurisdiction of its organization, and has all requisite power and authority, corporate or otherwise, to execute, deliver and perform this Agreement.

9.1.2 *Authorization*. The execution and delivery of this Agreement and the performance by it of the transactions contemplated hereby have been duly authorized by all necessary corporate action and do not violate (a) such Party's charter documents, bylaws or other organizational documents, (b) in any material respect, any agreement, instrument or contractual obligation to which such Party is bound, (c) any requirement of any Applicable Laws or (d) any order, writ, judgment, injunction, decree, determination or award of any court or governmental agency presently in effect applicable to such Party.

9.1.3 *Binding Agreement*. This Agreement is a legal, valid and binding obligation of such Party enforceable against it in accordance with its terms and conditions, subject to the effects of bankruptcy, insolvency or other laws of general application affecting the enforcement of creditor rights, judicial principles affecting the availability of specific performance and general principles of equity (whether enforceability is considered a proceeding at law or equity).

9.1.4 *No Inconsistent Obligation*. It is not under any obligation, contractual or otherwise, to any Person that conflicts with or is inconsistent in any material respect with the terms of this Agreement or that would impede the diligent and complete fulfillment of its obligations hereunder.

9.1.5 *No Debarment*. It shall not use in any capacity, in connection with the performance of the activities contemplated by this Agreement, any Person who has been debarred pursuant to Section 306 of the FDCA, or who is the subject of a conviction described in such section. It agrees to inform the other Party in writing immediately if it or any Person who is performing services hereunder on its behalf is debarred or is the subject of a conviction described in Section 306, or if any action, suit, claim, investigation or legal or administrative proceeding is pending or, to its Knowledge, is threatened, relating to the debarment or conviction of it or any Person performing services hereunder.

9.2 **Additional Representations of Targacept**. Targacept further represents and warrants to AstraZeneca, as of the Execution Date, and covenants, as follows:

9.2.1 The Existing Patent Rights are the only Targacept Patent Rights existing as of the Execution Date. To Targacept's Knowledge, no issued patents included in the Existing Patent Rights are invalid or unenforceable.

9.2.2 There are no claims, judgments or settlements against, or amounts with respect thereto owed by, Targacept or any of its Affiliates relating to the Regulatory Documentation, the Existing Patent Rights or the Targacept Know-How. No claim or litigation has been brought or threatened in writing by any Person alleging that (a) the Existing Patent Rights are invalid or unenforceable or (b) the Regulatory Filings, the Existing Patent Rights or the Targacept Know-How or the disclosing, copying, making, assigning or licensing of the Regulatory Filings, the Existing Patent Rights or the Targacept Know-How, or Developing or Commercializing Compound or Licensed Products as set forth herein violates, infringes or otherwise conflicts or interferes with any intellectual property or proprietary right of any Person.

9.2.3 Targacept is: (a) the sole and exclusive owner of the Existing Patent Rights listed on Schedule 2, Part A (the "**Owned Patent Rights**"); and (b) to Targacept's Knowledge, the sole and exclusive licensee of the Existing Patent Rights listed on Schedule 2, Part B (the "**In-Licensed Patent Rights**") with respect to the Primary Compound, the Racemic Compound, (1S, 2R, 4R)-N,2,3,3-tetramethylbicyclo[2.2.1]heptan-2-amine and Licensed Products that contain or are comprised of any of the foregoing, except for rights of the U.S. government and rights reserved by USFRF and Yale; in each case (clauses (a) and (b)) free of any encumbrance, lien or claim of ownership by any Third Party arising from the action or inaction of Targacept. The Owned Patent Rights and In-Licensed Patent Rights constitute all of the Existing Patent Rights. Targacept is entitled to grant the licenses and sublicenses specified in this Agreement.

9.2.4 To Targacept's Knowledge, the Development or Commercialization of any Compound or Licensed Product will not be subject to any other license or agreement to which Targacept or any of its Affiliates is a party other than the Targacept Sublicense Agreements, the Targacept Existing API Agreements and the ******** Agreement.

9.2.5 During the Term, Targacept shall: (a) not encumber or diminish the rights granted to AstraZeneca hereunder with respect to the Targacept Patent Rights, including by (i) committing any acts or permitting the occurrence of any omissions that would cause the breach or termination of the USFRF Agreement or the Yale Agreement or (ii) amending or otherwise modifying or permitting to be amended or modified, the USFRF Agreement or the Yale Agreement in a manner that would encumber or diminish the rights granted to AstraZeneca hereunder with respect to such Targacept Patent Rights; (b) without limitation of the foregoing clause (a) but subject to the proviso below, not ******** until the earlier of (i) the date on which AstraZeneca gives written consent, not to be unreasonably withheld, conditioned or delayed, or (ii) ******** days after ******** AstraZeneca; provided that, in the event AstraZeneca either gives such consent or does not provide written objection to ******** Targacept within such ******** day period, ******** shall be conclusively deemed not to ******** AstraZeneca hereunder with respect to the Targacept Patent Rights licensed by Targacept under the ********; and (c) promptly provide AstraZeneca with notice of any alleged breach by Targacept, or threatened or actual breach by USFRF or Yale, of the USFRF Agreement or the Yale Agreement.

9.2.6 To Targacept's Knowledge, the Existing Patent Rights have been filed and are being maintained in accordance with the procedures of the respective patent offices in which they are filed and all applicable fees have been paid.

9.2.7 Targacept has not previously assigned, transferred, licensed, conveyed or otherwise encumbered (including by granting any covenant not to sue with respect thereto) its right, title or interest in or to (a) the Existing Patent Rights, (b) Targacept Know-How as it relates specifically to the Primary Compound, Primary Compound Licensed Products or Regulatory Filings or (c) any Patent Rights or Information that would be (i) Existing Patent Rights or (ii) Targacept Know-How as it relates specifically to the Primary Compound, Primary Compound Licensed Products or Regulatory Filings but for such assignment, transfer, license, conveyance or encumbrance, except in each case ((clauses (a), (b) and (c)) where such assignment, transfer, license, conveyance or encumbrance is terminated and no longer in force or effect; and Targacept will not enter into any such agreements or grant any such right, title or interest to any Person that is inconsistent with the rights and licenses granted to AstraZeneca under this Agreement.

9.2.8 To Targacept's Knowledge, no Person is (a) infringing or threatening to infringe the Existing Patent Rights or (b) misappropriating or threatening to misappropriate the Targacept Know-How as it relates specifically to any Compound or Licensed Product.

9.2.9 True, complete and correct copies (as of the Execution Date) of: (a) the file wrapper relating to the prosecution and maintenance of the Owned Patent Rights and, to the extent in Targacept's possession, the In-Licensed Patent Rights; (b) the Targacept Sublicense Agreements, the Existing TRGT API Agreements, the ******** Agreement and, to Targacept's Knowledge, the USF/USFRF Agreement; (c) all Regulatory Filings (excluding drafts) with respect to the Primary Compound; and (d) all material adverse information with respect to the safety and efficacy of the Primary Compound Known to Targacept have been provided or made available (except to the extent publicly available) to AstraZeneca prior to the Execution Date.

9.2.10 Targacept has prepared, maintained and retained all Regulatory Filings in accordance in all material respects with Applicable Laws.

9.2.11 None of Targacept, any of its Affiliates or, to Targacept's Knowledge, any Third Party is in breach of a Targacept Sublicense Agreement, the Existing TRGT API Agreements or the ******** Agreement in any material respect and, to the Knowledge of Targacept, each of the Targacept Sublicense Agreements, the Existing TRGT API Agreements, the ******** Agreement and the USF/USFRF Agreement is in full force and effect.

9.2.12 To Targacept's Knowledge, the conduct of the Development Program and the Parties' Development of the Primary Compound and Primary Compound Licensed Products for which the Primary Compound is the sole active pharmaceutical ingredient in accordance with the Amplixa Global Development Outline and the first Amplixa Annual Global Development Plan, in each case as agreed as of the Execution Date, and the commercial sale by AstraZeneca of Primary Compound Licensed Products for which the Primary Compound is the sole active pharmaceutical ingredient as an Adjunct Therapy or a Monotherapy hereunder will not infringe any Patent Rights of any Person.

9.2.13 To Targacept's Knowledge, the conception, development and reduction to practice of (a) the Existing Patent Rights and (b) the Targacept Know-How existing as of the Execution Date as it relates specifically to any Compound or Licensed Products, in each case (clause (a) and (b)) have not constituted or involved the misappropriation of trade secrets or other rights or property of any Person.

9.2.14 In respect of the pending United States patent applications included in the Existing Patent Rights, Targacept has disclosed to the applicable Patent Examiner at the United States Patent and Trademark Office all references, documents, or information of which Targacept has Knowledge that would reasonably be expected to be required by Applicable Laws to be disclosed by Targacept to such Patent Examiner.

9.2.15 To Targacept's Knowledge, the Existing Patent Rights represent all Patent Rights within Targacept's or any of its Affiliates' ownership or Control that claim or cover Compounds or Licensed Products as of the Execution Date.

9.2.16 To Targacept's Knowledge, each of the Existing Patent Rights properly identifies each and every inventor of the claims thereof as determined in accordance with the laws of the jurisdiction in which such Existing Patent Rights are issued or such application is pending.

9.2.17 To Targacept's Knowledge, each Person who has or has had any ownership rights in or to any Owned Patent Rights has assigned and has executed an agreement assigning its entire right, title and interest in and to such Owned Patent Rights to Targacept.

9.2.18 No rights or licenses are required under the Existing Patent Rights or Targacept Know-How for the conduct of the Development Program or the Parties' Development of Compounds and Licensed Products in accordance with the Amplixa Global Development Outline and the first Amplixa Annual Global Development Plan, in each case as agreed as of the Execution Date, and the commercial sale by AstraZeneca of Primary Compound Licensed Products for which the Primary Compound is the sole active pharmaceutical ingredient as an Adjunct Therapy or a Monotherapy, other than those granted under Section 4.1.1.

9.2.19 To Targacept's Knowledge, all rights in all inventions and discoveries, made, developed or conceived by any employee or independent contractor of Targacept during the course of their employment (or other retention) by Targacept that are the subject of one or more Owned Patent Rights have been or will be assigned in writing to Targacept.

9.2.20 Targacept has obtained the right (including under any Patent Rights and other intellectual property rights) to use all Information, Inventions, Proprietary Materials and all other materials (including any formulations and manufacturing processes and procedures) developed or delivered by any Third Party under any agreements between Targacept and any such Third Party with respect to the Primary Compound and licensed to AstraZeneca hereunder, and Targacept has the rights under each such agreement to transfer such Information, Inventions, Proprietary Materials or other materials to AstraZeneca and its designees and to grant AstraZeneca the right to use such Information, Inventions, Proprietary Materials or other materials in the Development or Commercialization of the Primary Compound or any Primary Compound Licensed Product for which the Primary Compound is the sole active pharmaceutical ingredient without restriction; provided that, notwithstanding the foregoing, Targacept makes no representation or warranty with regard in any respect to the Information or Inventions of, or obtained from, either or both of ******** and ******** (including any ******** or ********), and all such Information and Inventions are expressly excluded in all respects from this Section 9.2.20.

9.2.21 To Targacept's Knowledge, the Targacept Know-How that constitutes Confidential Information subject to Section 8.2 has been kept confidential in all material respects or has been disclosed to Third Parties only under terms of confidentiality. To Targacept's Knowledge, no breach of such confidentiality has been committed by any Third Party.

9.2.22 All written information, documentation and other materials furnished or made available by Targacept upon the request of AstraZeneca during AstraZeneca's period of diligence prior to the Execution Date are true, complete and correct copies of what they purport to be.

9.2.23 Except as provided in the Targacept Sublicense Agreements, the Targacept Existing API Agreements and the ******** Agreement, there are no amounts that will be required to be paid to a Third Party as a result of the Development or Commercialization of the Primary Compound or Primary Compound Licensed Products for which the Primary Compound is the sole active pharmaceutical ingredient that arise out of any agreement to which Targacept is a party or, to Targacept's Knowledge, at all.

9.2.24 Targacept has obtained the consent of USFRF attached as Schedule 8 hereto and the consent of ******** attached as Schedule 9 hereto.

9.2.25 Targacept has not sold or offered for sale the Racemic Compound in the ROW Territory.

9.2.26 To Targacept's Knowledge, the Inventions claimed or covered by the Existing Patent Rights licensed by Targacept from USFRF: (a) were not conceived, discovered, developed or otherwise made in connection with any research activities funded, in whole or in part, by the federal government of the United States or any agency thereof; (b) are not a "subject invention" as that term is described in 35 U.S.C. Section 201(f); and (c) are not otherwise subject to the provisions of the Bayh-Dole Act.

9.2.27 Targacept is the sole and exclusive owner of the Existing Trademarks free of any encumbrance, lien or claim of ownership by any Third Party and is entitled to assign the Existing Trademarks as provided herein.

9.2.28 None of Targacept, any of its Affiliates or, to Targacept's Knowledge, any Third Party is researching or developing any compound or product under the ******** specifically for use as ******** or ******** (or other term reflecting the ******** of ******** or ********) for the ********, and ******** the ******** Targacept shall not, and shall cause its Affiliates not to, research or develop any compound or product ******** the ******** specifically for use as ******** or ******** (or other term reflecting the ******** of ******** or ********) for the ********.

9.2.29 The representations and warranties of Targacept in this Agreement, and the information, documents and materials furnished to AstraZeneca in connection with its period of diligence prior to the Execution Date, do not, taken as a whole, (a) contain any untrue statement of a material fact or (b) omit to state any material fact Known to Targacept to be necessary to make the statements or facts contained therein, in light of the circumstances under which they were made, not misleading.

ARTICLE 10
INDEMNIFICATION AND DISCLAIMERS

10.1 **Indemnification of AstraZeneca by Targacept**. Targacept shall indemnify, defend and hold harmless AstraZeneca, its Affiliates, all of its and their respective directors, officers, employees and agents and all successors, heirs and assigns of any of the foregoing (collectively, the "**AstraZeneca Indemnitees**") from and against all liabilities, damages, losses and expenses (including reasonable attorneys' fees and expenses of litigation and investigation) (collectively, "**Losses**") incurred by or imposed upon the AstraZeneca Indemnitees, or any of them, as a result of or arising from claims, suits, actions, demands or judgments of Third Parties, including personal injury and product liability claims (collectively, "**Claims**"), arising out of: (a) the breach of this Agreement by Targacept; (b) the gross negligence or willful misconduct of any Targacept Indemnitee in connection with Targacept's performance of this Agreement; (c) the Development or Commercialization of any Compound or Licensed Product (including Inversine®) prior to the Effective Date by Targacept, any of its Affiliates or any Person expressly authorized by Targacept or any of its Affiliates to Develop or Commercialize such Compound or Licensed Product; (d) the Development or Commercialization of any Compound or Licensed Product in a Terminated Territory (after termination of this Agreement with respect to such Terminated Territory) by Targacept, any of its Affiliates or any Person expressly authorized by Targacept or any of its Affiliates to Develop or Commercialize such Compound or Licensed Product; (e) the Development or Commercialization of any Compound or Licensed Product anywhere in the world (after termination of this Agreement in its entirety) by Targacept, any of its Affiliates or any Person expressly authorized by Targacept or any of its Affiliates to Develop or Commercialize such Compound or Licensed Product; (f) the Manufacture of any Licensed Product by or on behalf of Targacept pursuant to Section 3.3.4; (g) the failure of any supply of the Primary Compound or Primary Compound Licensed Product assigned to AstraZeneca pursuant to Section 3.3.3 to have been Manufactured (i) in compliance with the applicable specification with respect thereto as provided for in a purchase order submitted under the predecessor to the Existing TRGT Supply Agreement or in the ******** Agreement, as applicable, or (ii) in substantial compliance with Good Manufacturing Practices or other Applicable Laws; or (h) the adulteration or misbranding (within the meaning of the FDCA) of any supply of the Primary Compound or Primary Compound Licensed Product assigned to AstraZeneca pursuant to Section 3.3.3 or the inability under the FDCA to introduce such supply of Primary Compound or Primary Compound Licensed Product into interstate commerce; provided that, with respect to any Claim for which Targacept has an obligation to any AstraZeneca Indemnitee pursuant to this Section 10.1 and AstraZeneca has an obligation to any Targacept Indemnitee pursuant to Section 10.2, each Party shall indemnify each of the other Party's Indemnitees for its Losses to the extent of its responsibility, relative to the other Party, for the facts underlying such Claim.

10.2 **Indemnification of Targacept by AstraZeneca**. AstraZeneca shall indemnify, defend and hold harmless Targacept, its Affiliates, its and their respective directors, officers, employees and agents and all successors, heirs and assigns of any of the foregoing (collectively, the "**Targacept Indemnitees**") from and against all Losses incurred by or imposed upon the Targacept Indemnitees, or any of them, as result of or arising from Claims arising out of: (a) the Manufacture, use or sale in the Territory of any Compound or Licensed Product by (i) AstraZeneca, (ii) any of its Affiliates, (iii) any of its Sublicensees, Distributors, Net Sales Distributors or agents, or (iv) any Person expressly authorized by AstraZeneca or any of its Affiliates to do any of the foregoing; (b) the breach of this Agreement by AstraZeneca; or (c) the gross negligence or willful misconduct of any AstraZeneca Indemnitee in connection with AstraZeneca's performance of this Agreement; provided that with respect to any Claim for which Targacept has an obligation to any AstraZeneca Indemnitee pursuant to Section 10.1 and AstraZeneca has an obligation to any Targacept Indemnitee pursuant to this Section 10.2, each Party shall indemnify each of the other Party's Indemnitees for its Losses to the extent of its responsibility, relative to the other Party, for the facts underlying the Claim.

10.3 **Conditions to Indemnification**.

10.3.1 *Notice of Claim*. A Party seeking recovery (or defense) under this Article 10 (the "**Indemnified Party**") in respect of any Losses incurred by it or, in the case of AstraZeneca, one or more AstraZeneca Indemnitees or, in the case of Targacept, one or more Targacept Indemnitees (in either case, the "**Indemnitees**") shall give prompt notice of the applicable Claim (an "**Indemnification Claim Notice**") to the Party from which recovery (or defense) is sought (the "**Indemnifying Party**"), and in no event shall the Indemnifying Party be liable for any Losses that would not have occurred but for a failure in providing notice promptly. Each Indemnification Claim Notice must contain a description of the applicable Claim and the nature and amount of such Loss (to the extent that the nature and amount of such Loss is known at such time). The Indemnified Party shall furnish promptly to the Indemnifying Party copies of all papers and official documents received in respect of any Claims. All indemnification claims in respect of a Party or its Indemnitees shall be made solely by such Party.

10.3.2 *Claim Indemnification Procedures*. The obligations of an Indemnifying Party under this Article 10 with respect to Claims and Losses that are subject to Section 10.1 or Section 10.2 shall be governed by and be contingent upon the following additional terms and conditions:

(a) Subject to Section 7.12.2 and Section 7.12.3, at its option, the Indemnifying Party may assume the defense of any Claim by giving written notice to the Indemnified Party within ************ days after the applicable Indemnification Claim Notice is delivered to the Indemnifying Party. The assumption of the defense of a Claim by the Indemnifying Party shall not be construed as an acknowledgment that the Indemnifying Party is liable to indemnify the Indemnified Party or any of its Indemnitees in respect of such Claim, nor shall it constitute a waiver by the Indemnifying Party of any defenses it may assert against the Indemnified Party's, or any of its Indemnitees', claim for indemnification. Upon assuming the defense of a Claim, the Indemnifying Party may select and appoint lead counsel in the defense of the Claim, such lead counsel to be subject to the approval of the Indemnified Party (not to be unreasonably withheld, conditioned or delayed). In the event the Indemnifying Party assumes the defense of a Claim, the Indemnified Party shall promptly deliver to the Indemnifying Party all original notices and documents (including court papers) received by the Indemnified Party or any of its Indemnitees in connection with such Claim. If the Indemnifying Party assumes the defense of a Claim, except as provided in Section 10.3.2(b), the Indemnifying Party shall not be liable to the Indemnified Party or any of its Indemnitees for any legal expenses subsequently incurred by such Indemnified Party or Indemnitee(s) in connection with the analysis, defense or settlement of such Claim. In the event that it is judicially determined (in a final, non-appealable decision), or otherwise agreed by the Parties, that the Indemnifying Party is not obligated to indemnify, defend or hold harmless an Indemnified Party or any of its Indemnitee(s) from and against a Claim, the Indemnified Party shall reimburse the Indemnifying Party for any and all actual costs and expenses (including reasonable attorneys' fees and costs of suit) and Losses actually paid by the Indemnifying Party in its defense of such Claim with respect to such Indemnified Party or such Indemnitee(s).

(b) Without limitation of Section 10.3.2(a), if the Indemnifying Party assumes the defense of a Claim, the Indemnified Party and its Indemnitees shall be entitled to participate in, but not control, the defense of such Claim and to employ counsel of its choice for such purpose; provided that such employment shall be at the Indemnified Party's, or its Indemnitee's own expense unless (i) the employment thereof has been specifically authorized by the Indemnifying Party in writing, or (ii) the named parties to such Claim include both the Indemnifying Party and the Indemnified Party and the Indemnified Party reasonably concludes, based on advice from counsel, that the Indemnifying Party and the Indemnified Party have conflicting interests with respect to such Claim.

(c) With respect to each Claim for which the Indemnifying Party has assumed the defense in accordance with Section 10.3.2(a) and has acknowledged in writing the obligation to indemnify the Indemnified Party or any of its Indemnitees hereunder, the Indemnifying Party shall have the sole right to consent to the entry of any judgment, enter into any settlement or otherwise dispose of such Claim, on such terms as the Indemnifying Party, in its sole discretion, shall deem appropriate, provided such judgment, settlement or disposition does not result in the Indemnified Party or any of its Indemnitees becoming subject to injunctive or other relief or admitting fault or liability. With respect to each Claim for which the Indemnifying Party has assumed the defense of in accordance with Section 10.3.2(a) and has acknowledged in writing the obligation to indemnify the Indemnified Party or any of its Indemnitees hereunder, but as to which the immediately preceding sentence does not apply, the Indemnifying Party shall have authority to consent to the entry of any judgment, enter into any settlement or otherwise dispose of such Claim provided it obtains the prior written consent of the Indemnified Party (which consent shall not be unreasonably withheld, conditioned or delayed).

(d) The Indemnifying Party shall not be liable for any settlement or other disposition of a Claim by the Indemnified Party or any of its Indemnitees that is reached without the written consent of the Indemnifying Party.

(e) If the Indemnifying Party assumes the defense of any Claim, neither the Indemnified Party nor its Indemnitees shall admit any liability with respect to, or settle, compromise or discharge (other than as a result of a court-imposed judgment), such Claim without the prior written consent of the Indemnifying Party.

(f) If the Indemnifying Party chooses to assume control of the defense of any Claim, the Indemnified Party shall, and shall use diligent efforts to cause each of its Indemnitees to, (i) cooperate in all reasonable respects in the defense or prosecution thereof, (ii) furnish such records, information and testimony, (iii) provide such witnesses and (iv) attend such conferences, discovery proceedings, hearings, trials and appeals as may be reasonably requested in connection therewith. The Indemnifying Party shall reimburse the Indemnified Party and each of its Indemnitees for all its reasonable out-of-pocket expenses in connection with the foregoing.

10.4 **Insurance**.

10.4.1 *General*. AstraZeneca shall have and maintain such type and amounts of liability insurance covering the Manufacture, supply, use and sale of Compounds and Licensed Products as is normal and customary in the pharmaceutical industry for a Person of comparable size and engaged in activities comparable to the activities in which AstraZeneca engages hereunder. AstraZeneca's liability insurance shall be primary to any liability insurance carried by Targacept, which insurance shall be excess and non-contributory, for claims and losses to the extent arising out of AstraZeneca's performance of this Agreement and shall be specifically endorsed to list Targacept as an additional insured.

10.4.2 *Targacept*. Targacept shall maintain (a) commercial general liability insurance covering bodily injury and property damage with minimum limits of ******** Dollars (US $********) per occurrence and ******** Dollars (US $********) general aggregate, (b) commercial automobile liability insurance, if and for so long as Targacept has personnel located at the offices of AstraZeneca's Affiliate as contemplated by Section 3.2.3, covering owned, hired and non-owned vehicles with limits of at least ******** Dollars (US $********) combined single limit (bodily injury and property damage) and (c) products liability/completed operations coverage with minimum limits of ******** Dollars (US $********) each occurrence and ******** Dollars (US $********) general aggregate or, if Targacept is Commercializing a Compound or Licensed Product in any Terminated Territory (in the event this Agreement is terminated with respect to one or more Terminated Territories pursuant to Section 11.2.2) or anywhere in the world (in the event this Agreement is terminated in its entirety), ******** Dollars (US $********) per occurrence and ******** Dollars (US $********) general aggregate. Each of the above policies of insurance: (i) shall cover claims arising out of Targacept's performance of this Agreement that are made within a period of at least ******** years after the Term and claims arising out of Targacept's Commercialization of any Compound or Licensed Product in any Terminated Territory (in the event this Agreement is terminated with respect to one or more Terminated Territories pursuant to Section 11.2.2) or anywhere in the world (in the event this Agreement is terminated in its entirety), as applicable, that are made within a period of at least ******** years after the end of any such period in which Targacept is Commercializing any Compound or Licensed Product in any Terminated Territory (in the event this Agreement is terminated with respect to one or more Terminated Territories pursuant to Section 11.2.2) or anywhere in the world (in the event this Agreement is terminated in its entirety), as applicable; and (ii) shall be primary to any liability insurance carried by AstraZeneca, which insurance shall be excess and non-contributory, for claims and losses to the extent arising out of Targacept's performance of this Agreement. The general, commercial automobile (if any) and product liability policies shall be specifically endorsed to list AstraZeneca as an additional insured. In addition, Targacept shall maintain worker's compensation insurance as required by all applicable laws and employers liability coverage of not less than ******** Dollars (US $********). At such times as AstraZeneca may reasonably request in writing, Targacept shall provide AstraZeneca with a certificate of insurance evidencing the insurance coverage required under this Section 10.4.2, which certificate shall provide at least ******** days' notice of cancellation or termination of such insurance coverage. Such policies shall remain in effect throughout the Term and for ******** years thereafter and throughout any period during which Targacept is Commercializing any Compound or Licensed Product in any Terminated Territory (in the event this Agreement is terminated with respect to one or more Terminated Territories pursuant to Section 11.2.2) or anywhere in the world (in the event this Agreement is terminated in its entirety), as applicable and for ******** years thereafter, and shall not be canceled, if not replaced, without the prior written authorization of AstraZeneca. Maintenance of such insurance coverage shall not relieve Targacept of any responsibility under this Agreement for damages in excess of insurance limits or otherwise. All such insurance shall be written with a company or companies having a financial rating of not less than ******** in the most current edition of Best's Key Rating Guide.

10.5 **Warranty Disclaimer**. EXCEPT AS OTHERWISE EXPRESSLY PROVIDED IN THIS AGREEMENT, NEITHER PARTY MAKES ANY WARRANTY WITH RESPECT TO ANY TECHNOLOGY, PRODUCTS OR OTHER GOODS, SERVICES, RIGHTS OR OTHER SUBJECT MATTER OF THIS AGREEMENT AND EACH PARTY HEREBY DISCLAIMS ALL WARRANTIES, EXPRESS OR IMPLIED, INCLUDING, WITHOUT LIMITATION, WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE AND NONINFRINGEMENT.

10.5.1 *No Warranty of Success*. Nothing contained in this Agreement shall be construed as a warranty, either express or implied, on the part of either Party that: (a) the Development Program will yield any Licensed Products or otherwise be successful or meet its goals, objectives, timelines or budgets; or (b) a Compound or Licensed Product can or will be successfully Developed or Commercialized.

10.6 **Limited Liability**. NOTWITHSTANDING ANYTHING TO THE CONTRARY IN THIS AGREEMENT, NEITHER PARTY SHALL BE LIABLE TO THE OTHER PARTY OR ANY OF ITS AFFILIATES FOR ANY SPECIAL, PUNITIVE, INDIRECT, INCIDENTAL OR CONSEQUENTIAL DAMAGES, INCLUDING, WITHOUT LIMITATION, LOST PROFITS OR LOST REVENUES ARISING OUT OF THIS AGREEMENT OR THE PERFORMANCE THEREOF, WHETHER UNDER ANY CONTRACT, WARRANTY, NEGLIGENCE, STRICT LIABILITY OR OTHER LEGAL OR EQUITABLE THEORY. THIS SECTION 10.6 SHALL NOT BE DEEMED TO LIMIT EITHER PARTY'S OBLIGATION UNDER SECTION 10.1 OR SECTION 10.2, IF APPLICABLE, TO INDEMNIFY AND HOLD HARMLESS THE OTHER PARTY FROM AND AGAINST "LOSSES" ACTUALLY PAID BY SUCH OTHER PARTY TO THIRD PARTIES.

ARTICLE 11
TERM AND TERMINATION

11.1 **Term**. This Agreement shall become effective as of the Effective Date and, unless earlier terminated pursuant to this Article 11 or by mutual agreement of the Parties, shall continue in force and effect until the date, following expiration of the last Royalty Term for the last Licensed Product, of final payment to Targacept of all payment obligations of AstraZeneca under this Agreement (the period during which this Agreement is in force and effect, the "**Term**").

11.1.1 *Effect of Expiration of the Term*. Following the expiration of the Term, subject to the terms and conditions of this Agreement, AstraZeneca shall have a non-exclusive, fully-paid and royalty-free right and license, with the right to grant sublicenses (through multiple tiers), under the Targacept Technology as it exists as of the date of expiration solely to Develop and Commercialize Compound and Licensed Products in the Field in the Territory.

11.2 **Termination for Cause**.

11.2.1 *Material Breach*. Subject to Section 11.2.2, either Party (the "**Non-Breaching Party**") may, without prejudice to any other remedies available to it at law or in equity, terminate this Agreement in its entirety in the event (a) the other Party (the "**Breaching Party**") shall have materially breached the performance of any of its material obligations hereunder and (b) such breach shall have continued for ******** days (or, in the case of a payment breach, ******** days) after written notice thereof to the Breaching Party referencing this Section 11.2.1, describing in reasonable detail the alleged material breach and stating its intention to pursue a remedy under this Section 11.2.1 if not cured; provided that, except in the case of a payment breach and except as provided in Section 11.2.3, if the Breaching Party has during such ******** day period commenced and diligently continued conducting activities designed to cure such breach but such cure is not possible during such ******** day period, the Breaching Party shall have an additional ******** days in which to cure such breach. Subject to Section 11.2.3, termination of this Agreement by the Non-Breaching Party shall become effective on the last day of the applicable cure period if the alleged breach has not been cured.

11.2.2 *Material Breach Related to Diligence in* ********. Notwithstanding Section 11.2.1, if the material breach and failure to cure contemplated by Section 11.2.1 is with respect to any of AstraZeneca's obligations under clause ******** of Section ******** with respect to ******** but not ********, Targacept shall have the right to terminate this Agreement ******** with respect to ********.

11.2.3 *Disagreement.* If the Parties in good faith dispute whether there has been a material breach as alleged pursuant to Section 11.2.1 (including as described in Section 11.2.2) or whether such material breach has been cured or cured on a timely basis, either Party shall have the right to initiate dispute resolution in accordance with Section 12.1 to resolve such dispute. If the Breaching Party initiates such dispute resolution procedure during the cure period set forth in Section 11.2.1 to resolve the dispute for which termination is being sought and is diligently pursuing such procedure, the cure period set forth in Section 11.2.1 shall be tolled and the termination shall become effective only if such breach remains uncured for ******** days (or, in the case of a payment breach, ******** days) after the final resolution of the dispute through such dispute resolution procedure This Section 11.2 defines exclusively the Parties' right to terminate in case of any material breach of contract.

11.3 **Unilateral Termination Rights**.

11.3.1 *AstraZeneca - Entire Agreement.* AstraZeneca shall have the right to terminate this Agreement in its entirety, without incurring any additional liability, penalty, cost or expense to Targacept, other than any costs or expenses that are (x) accrued as of the effective date of such termination (including, for clarity, during the applicable notice period) or (y) otherwise provided for in this Article 11:

(a)******** if, after the JDC and Executive Officers meeting required as set forth below, AstraZeneca determines in good faith that it is not advisable for AstraZeneca to continue to Develop or Commercialize Compounds or Licensed Products as a result of a perceived serious safety issue regarding the use of the Primary Compound, immediately upon written notice to Targacept; provided that, if AstraZeneca perceives there to be such a serious safety issue: (i) AstraZeneca shall notify Targacept and the JDC and the Executive Officers shall meet as soon as practicable thereafter in person; and (ii) at such meeting, AstraZeneca shall (A) provide the JDC and the Executive Officers with any ******** and ******** related to the Primary Compound not previously provided in writing by AstraZeneca to Targacept that demonstrates such perceived serious safety issue and (B) explain in detail to the JDC and the Executive Officers the basis for AstraZeneca's good faith belief, including the supporting factors, and, if applicable, Targacept's members of the JDC and Executive Officer may provide to AstraZeneca any ******** and ******** that supports a contrary belief of Targacept;

(b) in its sole discretion upon at least ******** days' written notice to Targacept, which notice must be given to Targacept (i) no sooner than ******** days after ******** of the last to be completed Phase 3 Clinical Trial designed to support an NDA (the first NDA) for the Milestone Product and (ii) no later than ******** days after such ********; provided that, notwithstanding anything herein to the contrary, AstraZeneca shall not be required to ******** any ******** with respect to a Licensed Product after giving notice of termination referencing this Section 11.3.1(b); or

(c) immediately upon written notice to Targacept in the event that AstraZeneca both: (i) reasonably believes, having obtained the advice of independent patent counsel, that the Commercialization of the Primary Compound or Primary Compound Licensed Products for which the Primary Compound is the sole active pharmaceutical ingredient by AstraZeneca, any of its Affiliates or any of its or their Sublicensees is more likely than not to infringe or misappropriate any Patent Rights, trade secrets or any other intellectual property right of a Third Party(ies) in either the U.S. Territory or at least two (2) Major Countries, such that it is more likely than not that AstraZeneca, any of its Affiliates or any of its or their Sublicensees would not be able to Commercialize the Primary Compound or Primary Compound Licensed Products for which the Primary Compound is the sole active pharmaceutical ingredient in the U.S. Territory or such Major Countries, as applicable, without infringing such Patent Rights or other intellectual property right of such Third Party; and (ii) is unable to obtain a license from such Third Party(ies) on commercially reasonable terms.

In addition, notwithstanding anything herein to the contrary, if AstraZeneca terminates this Agreement with respect to the United States (i.e., the U.S. Territory) pursuant to Section 11.3.2, this Agreement shall automatically terminate in its entirety as of the effective date of termination with respect to the U.S. Territory.

11.3.2 *AstraZeneca - With Respect to a Major Country.* AstraZeneca shall have the right to terminate this Agreement in its sole discretion with respect to each Major Country, on a Major Country-by-Major Country basis, without incurring any additional liability, penalty, cost or expense to Targacept, other than any costs or expenses that are (a) accrued as of the effective date of such termination (including, for clarity, during the applicable notice period) or (b) otherwise provided for in this Article 11, upon ******** days' written notice to Targacept specifying the applicable Major Country and referencing this Section 11.3.2; provided that no such termination pursuant to this Section 11.3.2 shall be permitted or effective prior to the fourth (4th) anniversary of the Effective Date.

11.3.3 *Targacept.* Except to the extent the following is unenforceable under the law of a particular jurisdiction where a patent application within the Targacept Patent Rights or Targacept Program Patent Rights is pending or a patent within the Targacept Patent Rights or Targacept Program Patent Rights issued, Targacept may terminate this Agreement in its entirety immediately on written notice to AstraZeneca in the event that AstraZeneca or any of its Affiliates or any of its or their Sublicensees Challenges any Targacept Patent Rights or Targacept Program Patent Rights or assists a Third Party in initiating a Challenge of any Targacept Patent Rights or Targacept Program Patent Rights; provided that, if such Challenge is by a Sublicensee of AstraZeneca or any of its Affiliates, Targacept shall notify AstraZeneca of such Challenge and may not terminate this Agreement if AstraZeneca notifies Targacept within ******** Business Days after the receipt of such notice that it (or its applicable Affiliate) has a valid right to terminate and will terminate the Sublicensee's sublicense and then provides written notice of such termination to Targacept within ******** Business Days thereafter.

11.4 **Termination for Insolvency**.

11.4.1 *Right to Terminate*. In the event that either Party files for protection under bankruptcy or insolvency laws, makes an assignment for the benefit of creditors, appoints or suffers appointment of a receiver or trustee over substantially all of its property that is not discharged within ******** days after such filing, proposes a written agreement of composition or extension of its debts, proposes or is a party to any dissolution or liquidation (other than in connection with a Change of Control of such Party that does not result in the dissolution or liquidation or other similar event by the successor to such Party), files a petition under any bankruptcy or insolvency act or has any such petition filed against that is not discharged within ******** days of the filing thereof, then the other Party may terminate this Agreement in its entirety effective immediately upon written notice to such Party that specifically references this Section 11.4.1.

11.4.2 *Rights and Licenses*. The Parties intend that all rights and licenses granted under or pursuant to any section of this Agreement are and shall otherwise be deemed to be for purposes of Section 365(n) of Title 11, United States Code (the "**Bankruptcy Code**"), or any analogous provisions in any country or jurisdiction in the ROW Territory, licenses of rights to "intellectual property" as defined in Section 101(35A) of the Bankruptcy Code. The Parties shall retain and may fully exercise all of their respective rights and elections under the Bankruptcy Code, or any analogous provisions in any country or jurisdiction in the ROW Territory. To the extent lawful, upon the bankruptcy of either Party, the non-bankrupt Party shall further be entitled to a complete duplicate of, or complete access to, any such intellectual property in tangible form, and such, if not already in its possession, shall be promptly delivered to the non-bankrupt Party, unless the bankrupt Party elects to continue, and continues, to perform all of its obligations under this Agreement.

11.5 **Effect of Certain Terminations**.

11.5.1 In the event of a termination of this Agreement in its entirety by AstraZeneca pursuant to Section 11.3.1(b) or (c), by Targacept pursuant to Section 11.2.1, 11.3.3 or 11.4.1 or as provided in the last sentence of Section 11.3.1:

(a) all rights and licenses granted by Targacept hereunder shall immediately terminate;

(b) all rights and licenses granted by AstraZeneca pursuant to Section 4.1.2 hereunder shall immediately terminate;

(c) AstraZeneca shall, and hereby does effective as of the date of termination, grant Targacept and its Affiliates an exclusive license, with the right to grant sublicenses (through multiple tiers), under AstraZeneca Termination Technology (excluding Product Information, which shall be assigned to Targacept as set forth in Section 11.5.1(d)) Controlled by AstraZeneca as of the effective date of such termination to Develop and Commercialize in the Field in the entire world, itself or through contractors, Compounds and Licensed Products; provided that: (i) the foregoing license shall exclude any license or other rights with respect to any ******** that is not a ******** and the ******** of which is covered by Patent Rights owned or Controlled by AstraZeneca; (ii) AstraZeneca shall provide Targacept with copies of any and all AstraZeneca Third Party Agreements with respect to the AstraZeneca Termination Technology that is the subject of the license granted by AstraZeneca to Targacept pursuant to this Section 11.5.1(c) and Targacept may at any time thereafter exclude all of the AstraZeneca Termination Technology that is the subject of any such AstraZeneca Third Party Agreement from the grant set forth in this Section 11.5.1(c) by written notice to AstraZeneca, in which event clauses (iii), (v) and (vi) below shall not apply thereafter to such AstraZeneca Third Party Agreement and, for clarity, Targacept shall have no obligations with respect to any amounts that may become payable under such AstraZeneca Third Party Agreement; (iii) Targacept shall be responsible for (A) making any payments (including royalties, milestones and other amounts) payable by AstraZeneca to Third Parties under any such AstraZeneca Third Party Agreements that are applicable to the grant to Targacept of such license or to the exercise of such license by Targacept or any of its Affiliates or Sublicensees, by making such payments directly to AstraZeneca and, in each instance, Targacept shall make the requisite payments to AstraZeneca and provide the necessary reporting information to AstraZeneca in sufficient time to enable AstraZeneca to comply with its obligations under the AstraZeneca Third Party Agreements, and (B) complying with any other obligations included in any such AstraZeneca Third Party Agreements that are applicable to the grant to Targacept of such license or to the exercise of such license by Targacept or any of its Affiliates or Sublicensees; (iv) AstraZeneca shall be responsible for paying or providing to any such Third Party any payments or reports made or provided by Targacept under this Section 11.5.1(c); (v) AstraZeneca shall not amend any such AstraZeneca Third Party Agreement in any manner that encumbers or diminishes the rights granted to Targacept pursuant to this Section 11.5.1(c) without Targacept's prior written consent, not to be unreasonably withheld, conditioned or delayed, and AstraZeneca shall not undertake any action that would allow a Third Party to terminate any such AstraZeneca Third Party Agreement; and (vi) AstraZeneca shall, if reasonably requested to do so by Targacept, promptly enter into confirmatory license agreements in the form or substantially the form set out in Schedule 7 attached hereto (with the Parties reversed) for purposes of recording the licenses granted under this Agreement with such patent offices in the Territory as Targacept considers reasonably necessary, including to avoid disclosure of this Agreement; provided that, as between the Parties, regardless of whether any required confirmatory licenses are executed, the Parties' respective rights and obligations in respect of AstraZeneca Termination Technology shall be as set forth under this Agreement;

(d) to the extent requested in writing by Targacept, AstraZeneca shall promptly:

(i) assign all right, title and interest in and to any and all Product Information and, at Targacept's reasonable expense, execute all documents and do all proper actions reasonably required by Targacept from time to time to perfect Targacept's title to and ownership thereof;

(ii) where permitted by Applicable Laws, transfer to Targacept all of its right, title and interest in all Regulatory Documentation (including, for clarity, Product Regulatory Approvals) then in its name applicable to any Compound or Licensed Product in the Territory;

(iii) notify the applicable Regulatory Authorities and take any other action reasonably necessary to effect the transfer set forth in clause (ii) above;

(iv) unless expressly prohibited by any Regulatory Authority, transfer control to Targacept of all Clinical Studies of each Compound or Licensed Product being conducted as of the effective date of termination and continue to conduct such Clinical Studies, at Targacept's cost, for up to ******** months to enable such transfer to be completed without interruption of any such Clinical Study; provided that (A) for clarity, Targacept shall not have any obligation to continue any Clinical Study unless required by Applicable Laws and (B) with respect to each Clinical Study for which such transfer is expressly prohibited by the applicable Regulatory Authority, if any, AstraZeneca shall continue to conduct such Clinical Study to completion, at Targacept's reasonable cost;

(v) assign (or cause its Affiliates to assign) to Targacept all agreements with any Third Party with respect to the conduct of Preclinical Activities or Clinical Studies of each Compound or Licensed Product including agreements with contract research organizations, clinical sites and investigators, unless, with respect to any such agreement, such agreement (A) expressly prohibits such assignment, in which case AstraZeneca shall cooperate with Targacept in all reasonable respects to secure the consent of the applicable Third Party to such assignment, or (B) covers clinical trials for Combination Products in which any active pharmaceutical ingredient that is not a Compound is covered by Patent Rights of AstraZeneca or products covered by Patent Rights of AstraZeneca in addition to Licensed Products, in which case, AstraZeneca would be required, at Targacept's sole cost and expense, to cooperate with Targacept in all reasonable respects to facilitate the execution of a new agreement between Targacept and the applicable Third Party;

(vi) provide Targacept with all supplies of each Compound and all supplies of each Licensed Product owned by AstraZeneca or any Affiliate of AstraZeneca, wherever located, at a transfer price equal to (A) AstraZeneca's ******** (determined as provided on Schedule 10 attached hereto) plus ******** percent (*********%) or (B) if, with respect to any Compound or Licensed Product, AstraZeneca's supply is purchased from a Third Party, the actual costs paid by AstraZeneca or Targacept to such Third Party ********;

(vii) without limitation of clause (i) above, subject to any Third Party agreement, provide Targacept with copies of all reports and data generated or obtained by AstraZeneca or any of its Affiliates that relate to any Compound or Licensed Product that have not previously been provided to Targacept;

(viii) facilitate the orderly transition to Targacept of, and transition to Targacept, control of the Prosecution and Maintenance of all Targacept Patent Rights, Targacept Program Patent Rights and AstraZeneca Extended Term Patent Rights (and discuss with Targacept in good faith a likewise transition of control of the Prosecution and Maintenance of Joint Program Patent Rights) that AstraZeneca was Prosecuting and Maintaining as of the effective date of such termination and, in each case, meeting during such transition in a manner reasonably directed by Targacept all applicable deadlines needed to be met to establish or preserve such Patent Rights;

(ix) use diligent efforts in good faith to provide all documents with respect to Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Extended Term Patent Rights and Joint Program Patent Rights that Targacept may reasonably request in connection with any current or potential future effort to secure patent term extensions for Licensed Products; and

(x) assign to Targacept all right, title and interest of AstraZeneca in each Product Trademark;

(e) to the extent requested in writing by Targacept, AstraZeneca shall supply Targacept with its requirements for each Compound and its requirements for each Licensed Product (which amounts shall be consistent with AstraZeneca's historical usage thereof and then-current forecasts therefor) for up to ******** following such termination (i) at a transfer price equal to AstraZeneca's ******** (determined as provided on Schedule 10 attached hereto) ******** for the supply thereof or (ii) if, with respect to any Compound or Licensed Product, AstraZeneca's supply is purchased from a Third Party, at a transfer price equal to the actual costs paid by AstraZeneca or Targacept to such Third Party with respect to such supply of such Compound or Licensed Product ********; and, promptly after Targacept's request, AstraZeneca shall provide to Targacept or its designee all Information in its Control with respect to the Manufacture of each Compound and the Manufacture of each Licensed Product that is being researched, is in Development or is being Commercialized as of the effective date of such termination, solely in the forms, formulations or methods of delivery as such Compound or Licensed Product exists as of the effective date of such termination; and

(f) if this Agreement is terminated in its entirety by AstraZeneca pursuant to Section 11.3.1 or as provided in the last sentence of Section 11.3.1 and after the effective date of such termination Targacept or any of its Affiliates, Sublicensees or Net Sales Distributors Commercializes a Licensed Product that was the subject of a Clinical Study prior to or as of the effective date of such termination or was being Commercialized as of the effective date of such termination (each such Licensed Product, if any, a "**Reverse Royalty Territory Product**"), then within ******** days after the end of each Calendar Quarter (commencing with the Calendar Quarter in which the first sale (excluding "treatment IND sales," "named patient sales" and "compassionate use sales") of the first Reverse Royalty Territory Product for use or consumption by the general public in any country by Targacept or any of its Affiliates, (sub)licensees (including Sublicensees) or Net Sales Distributors after (a) this Section 11.5.1 becomes operative and (b) Regulatory Approval from the applicable Regulatory Authority has been obtained), Targacept shall pay AstraZeneca a royalty on Net Sales of each Reverse Royalty Territory Product in each country in the world by Targacept or any of its Affiliates or its or their licensees, Sublicensees or Net Sales Distributors at a rate of (x) ******** percent (********%), for each Reverse Royalty Territory Product with respect to which ******** of the ******** (as specified in the applicable ********) were ******** in at least ******** prior to AstraZeneca's notice of termination (******** or ******** to ********, as ********, for each such ********, using the ******** specified in the ********), if any, or (y) ********, for each Reverse Royalty Territory Product as to which clause (x) above does not apply. Targacept's obligation to pay royalties under this Section 11.5.1(f) shall expire with respect to each Reverse Royalty Territory Product in each country upon the later of:

(i) expiration of the last to expire Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Program Patent Rights, AstraZeneca Extended Term Patent Rights or Joint Program Patent Rights in such country that includes a Valid Claim that covers:

(A) the ******** of such Reverse Royalty Territory Product;

(B) a ******** or ******** such Reverse Royalty Territory Product (including the ******** of such Reverse Royalty Territory Product); or

(C) a ******** of such Reverse Royalty Territory Product for ******** for which such Reverse Royalty Territory Product has obtained Regulatory Approval (and, in the case of any country in which ******** or ******** is required, such ******** or ********) in such country, if, solely in the case of this clause (C), no ******** (other than a ******** or ******** of ********) is selling in such country a ******** that:

(1) is, if such country is the U.S. Territory, ******** in the ******** as a ******** that the ******** considers to be ******** such Reverse Royalty Territory Product; or

(2) is, if such country is outside of the U.S. Territory, ******** in the manner required by Applicable Laws in such country as ******** and ******** such Reverse Royalty Territory Product; and

(ii) ******** years from the First Commercial Sale of such Reverse Royalty Territory Product in such country (whether occurring before or after this Section 11.5.1 becomes operative).

During such period (if any) as Targacept is required to pay royalties to AstraZeneca pursuant to this Section 11.5.1(f), the definition of "Net Sales," "Net Sales Distributors," and Sections 5.3.1(c)(i-iv), 5.3.1(d), and 5.5 through 5.10 shall apply *mutatis mutandis* to the calculation (including credits and offsets), payment, recording and auditing of Targacept's obligations to pay royalties under this Section 11.5.1(f) as they apply to AstraZeneca and, solely for such purpose, each reference in each such Section (and any related definitions) to AstraZeneca shall be deemed to be a reference to Targacept.

11.5.2 In the event of a termination of this Agreement in its entirety by AstraZeneca pursuant to Section 11.3.1(a), Sections 11.5.1(a), (b), (c), (d) and (f) shall apply.

11.5.3 In the event of a termination of this Agreement with respect to a Terminated Territory by Targacept pursuant to Section 11.2.2 or by AstraZeneca pursuant to Section 11.3.2:

(a) all rights and licenses granted by Targacept hereunder (i) shall automatically be deemed to be amended to exclude, if applicable, the right to market, promote, detail, distribute, import, sell, offer for sale, file any Drug Approval Application for or seek any Product Regulatory Approval for any one or more Compounds or Licensed Products in such Terminated Territory and (ii) shall otherwise survive and continue in effect in such Terminated Territory solely for the purpose of furthering any Development or Commercialization of Compounds and Licensed Products in the Territory;

(b) all rights and licenses granted by AstraZeneca pursuant to Section 4.1.2 that relate solely to the Development of Compounds and Licensed Products in such Terminated Territory shall immediately terminate;

(c) AstraZeneca shall, and hereby does effective as of the date of termination, grant Targacept and its Affiliates an exclusive license, with the right to grant sublicenses (through multiple tiers), under AstraZeneca Termination Technology (excluding Product Information related solely to such Terminated Territory, which shall be assigned to Targacept as set forth in Section 11.5.3(d)) Controlled by AstraZeneca as of the effective date of such termination of this Agreement with respect to such Terminated Territory to Develop in the Field for such Terminated Territory and Commercialize in the Field in such Terminated Territory, itself or through contractors, Compounds and Licensed Products; provided that (i) the foregoing license shall exclude any license or other rights with respect to any ******** that is not a ******** and the ******** of which is covered by Patent Rights owned or Controlled by AstraZeneca; (ii) AstraZeneca shall provide Targacept with copies of all AstraZeneca Third Party Agreements with respect to AstraZeneca Termination Technology that is the subject of the license granted by AstraZeneca to Targacept pursuant to this Section 11.5.3(c) and Targacept may at any time thereafter exclude all of the AstraZeneca Termination Technology that is the subject of any such AstraZeneca Third Party Agreement from the grant set forth in this Section 11.5.3(c) by written notice to AstraZeneca, in which event clauses (iii), (v) and (vi) below shall not apply thereafter to such AstraZeneca Third Party Agreement and, for clarity, Targacept shall have no obligations with respect to any amounts that may become payable under such AstraZeneca Third Party Agreement; (iii) Targacept shall be responsible for (A) making any payments (including royalties, milestones and other amounts) payable by AstraZeneca to Third Parties under any such AstraZeneca Third Party Agreements that are applicable to the grant to Targacept of such license with respect to such Terminated Territory or to the exercise of such license by Targacept or any of its Affiliates or Sublicensees by making such payments directly to AstraZeneca and, in each instance, Targacept shall make the requisite payments to AstraZeneca and provide the necessary reporting information to AstraZeneca in sufficient time to enable AstraZeneca to comply with its obligations under any such AstraZeneca Third Party Agreements, and (B) complying with any other obligations included in any such AstraZeneca Third Party Agreements that are applicable to the grant to Targacept of such license with respect to such Terminated Territory or to the exercise of such license by Targacept or any of its Affiliates or Sublicensees; (iv) AstraZeneca shall be responsible for paying or providing to any such Third Party any payments or reports made or provided by Targacept under this Section 11.5.3(c); (v) AstraZeneca shall not amend any such AstraZeneca Third Party Agreements in any manner that encumbers or diminishes the rights granted to Targacept pursuant to this Section 11.5.3(c) without Targacept's prior written consent, not to be unreasonably withheld, conditioned or delayed, and AstraZeneca shall not undertake any action that would allow the Third Party to terminate any such AstraZeneca Third Party Agreement; and (vi) AstraZeneca shall, if reasonably requested to do so by Targacept, promptly enter into confirmatory license agreements in the form or substantially the form set out in Schedule 7 attached hereto (with the Parties reversed) for purposes of recording the licenses granted under this Agreement with such patent offices in the Territory as Targacept considers reasonably necessary, including to avoid disclosure of this Agreement; provided that, as between the Parties, regardless of whether any required confirmatory licenses are executed, the Parties' respective rights and obligations in respect of AstraZeneca Termination Technology shall be as set forth under this Agreement;

(d) to the extent requested in writing by Targacept, AstraZeneca shall promptly:

(i) assign all right, title and interest in and to any and all Product Information related solely to such Terminated Territory and, at Targacept's reasonable expense, execute all documents and do all proper actions reasonably required by Targacept from time to time to perfect Targacept's title to and ownership thereof; provided that all such assigned Product Information shall constitute Targacept Know-How from and after the effective date of such termination;

(ii) where permitted by Applicable Law, transfer to Targacept all of its right, title and interest in all Regulatory Documentation (including, for clarity, Product Regulatory Approvals) then in its name solely applicable to any Compound or Licensed Product that is in clinical development or is being Commercialized, as such Regulatory Documentation exists as of the effective date of such termination of this Agreement with respect to such Terminated Territory; provided that AstraZeneca retains a right of reference under any Regulatory Documentation transferred pursuant to this clause (ii) as necessary or reasonably useful for AstraZeneca to Develop or Commercialize Compound or Licensed Products in the Territory;

(iii) notify the applicable Regulatory Authorities and take any other action reasonably necessary to effect the transfer set forth in clause (ii) above;

(iv) without limitation of clause (i) above, subject to any Third Party agreement, provide Targacept with copies of all reports and data generated or obtained by AstraZeneca or any of its Affiliates that relate to any Compound or Licensed Product that have not previously been provided to Targacept;

(v) grant Targacept a right of reference to all Regulatory Documentation then in AstraZeneca's name that are not transferred to Targacept pursuant to clause (ii) above that are necessary or reasonably useful for Targacept, any of its Affiliates or Sublicensees to Develop or Commercialize any Compound or Licensed Product that is in clinical development or is being Commercialized, as such Regulatory Documentation exists as of the effective date of such termination of this Agreement with respect to such Terminated Territory;

(vi) facilitate the orderly transition to Targacept of, and transition to Targacept, control of the Prosecution and Maintenance of all Targacept Patent Rights, Targacept Program Patent Rights and AstraZeneca Extended Term Patent Rights (and discuss with Targacept in good faith a likewise transition of control of the Prosecution and Maintenance of Joint Program Patent Rights) that AstraZeneca was Prosecuting and Maintaining in or with respect to such Terminated Territory as of the effective date of such termination and, in each case, meeting during such transition in a manner reasonably directed by Targacept all applicable deadlines needed to be met to establish or preserve such Patent Rights;

(vii) use diligent efforts in good faith to provide all documents with respect to Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Extended Term Patent Rights and Joint Program Patent Rights in or with respect to such Terminated Territory that Targacept may reasonably request in connection with any current or potential future effort to secure patent term extensions for Licensed Products in such Terminated Territory; and

(viii) grant Targacept an exclusive (even as to AstraZeneca) license under the Product Trademarks to Commercialize Licensed Products in such Terminated Territory;

(e) to the extent requested in writing by Targacept, AstraZeneca shall supply Targacept with its requirements for each Compound and its requirements for each Licensed Product with respect to such Terminated Territory (which amounts shall be consistent with AstraZeneca's historical usage thereof and then-current forecasts therefor with respect to such Terminated Territory) for up to ******** months following such termination (i) at a transfer price equal to AstraZeneca's ******** (determined as provided on Schedule 10 attached hereto) ******** for the supply thereof or (ii) if, with respect to any Compound or Licensed Product, AstraZeneca's supply is purchased from a Third Party, at a transfer price equal to the actual costs paid by AstraZeneca or Targacept to such Third Party with respect to such supply of Compound or Licensed Product ********; and, promptly after Targacept's request, AstraZeneca shall provide to Targacept or its designee all Information in its Control with respect to the Manufacture of each Compound and the Manufacture of each Licensed Product that is being researched, is in Development or is being Commercialized with respect to such Terminated Territory as of the effective date of such termination, solely in the forms, formulations or methods of delivery as such Compound or Licensed Product exists as of the effective date of the termination of this Agreement with respect to such Terminated Territory;

(f) each Party shall provide the other Party on a timely basis with access to all material preclinical and clinical data compiled in support of any Product Regulatory Approval or other Regulatory Documentation with respect to Compounds or Licensed Products, in the case of Targacept, with respect to such Terminated Territory, and, in the case of AstraZeneca, with respect to the Territory; provided that the Party receiving such access shall not have the right to use any such data to support a Product Regulatory Approval for a product unless the inclusion of such data is required or advisable to comply with a requirement to report worldwide clinical studies to Regulatory Authorities in a filing a Drug Approval Application or seeking or maintaining a Product Regulatory Approval of a Licensed Product;

(g) promptly following the effective date of termination of this Agreement with respect to such Terminated Territory, the Parties shall enter into an agreement (or an amendment to the Safety Agreement) governing the Parties' respective rights and responsibilities with respect to the coordination of safety-related regulatory obligations, including the reporting of Adverse Events and other safety or quality data, which agreement shall set forth terms and conditions with respect to such activities that are reasonable and customary in the industry for agreements of that nature;

(h) to the extent permitted by Applicable Laws, each Party: (i) shall, and shall cause its Affiliates, distributors (including Distributors and Net Sales Distributors) and (sub)licensees (including Sublicensees) to, distribute, market, promote, offer for sale and sell Licensed Products only in the countries that it is permitted to do so under this Agreement (with respect to AstraZeneca, the Territory and, with respect to Targacept, the Terminated Territory), and (ii) shall not, shall not permit its Affiliates to, and shall require its distributors (including Distributors and Net Sales Distributors) and (sub)licensees (including Sublicensees) not to distribute, market, promote, offer for sale or sell Licensed Products (A) to any Person outside such countries or (B) to any Person inside such countries who (1) it has reason to believe is reasonably likely to distribute, market, promote, offer for sale or sell Licensed Products outside such countries or assist another Person to do so, or (2) it knows has previously distributed, marketed, promoted, offered for sale or sold Licensed Products outside such countries or assisted another Person to do so;

(i) if this Agreement is terminated with respect to such Terminated Territory by AstraZeneca pursuant to Section 11.3.2 (and, for clarity, not by Targacept pursuant to Section 11.2.2) and after the effective date of such termination Targacept or any of its Affiliates, Sublicensees or Net Sales Distributors Commercializes a Licensed Product in such Terminated Territory that was the subject of a Clinical Study prior to or as of the effective date of such termination or was being Commercialized in the Terminated Territory as of the effective date of such termination (each such Licensed Product, if any, a "**Reverse Royalty Terminated Territory Product**"), then within ******** days after the end of each Calendar Quarter (commencing with the Calendar Quarter in which the first sale (excluding "treatment IND sales," "named patient sales" and "compassionate use sales") of such Reverse Royalty Terminated Territory Product for use or consumption by the general public in such Terminated Territory by Targacept or any of its Affiliates, (sub)licensees (including Sublicensees) or Net Sales Distributors after (a) this Section 11.5.3 becomes operative and (b) Regulatory Approval from the applicable Regulatory Authority has been obtained), Targacept shall pay AstraZeneca a royalty on Net Sales of each Reverse Royalty Terminated Territory Product in the Terminated Territory by Targacept or any of its Affiliates or its or their licensees, Sublicensees or Net Sales Distributors at a rate of (x) ******** percent (*********%), for each Reverse Royalty Terminated Territory Product with respect to which ******** of the ******** (as specified in the applicable ********) were ******** in at least ******** prior to AstraZeneca's notice of termination (******** or ******** to ********, as ********, for each such ********, using the ******** specified in the *********), if any, or (y) ******** percent (*********%) for each Reverse Royalty Terminated Territory Product as to which clause (x) above does not apply. Targacept's obligation to pay royalties under this Section 11.5.3(i) shall expire with respect to each such Reverse Royalty Terminated Territory Product in such Terminated Territory upon the later of:

(i) expiration of the last to expire Targacept Patent Rights, Targacept Program Patent Rights, AstraZeneca Program Patent Rights, AstraZeneca Extended Term Patent Rights or Joint Program Patent Rights in such Terminated Territory that includes a Valid Claim that covers:

(A) the ******** of such ********;

(B) a ******** containing or comprising such Reverse Royalty Terminated Territory Product (including the pharmaceutical composition of such Reverse Royalty Terminated Territory Product); or

(C) a ******** of such Reverse Royalty Terminated Territory Product for any ******** for which such Reverse Royalty Terminated Territory Product has obtained Regulatory Approval (and if ******** or ******** is required in such Terminated Territory, such ******** or ********) in such country, if, solely in the case of this clause (C), no ******** (other than ******** or ******** of ********) is ******** in such Terminated Territory a ******** that is ******** in the manner required by Applicable Laws in such Terminated Territory as ******** and ******** such Reverse Royalty Terminated Territory Product; and

(ii) ******** years from the date of the First Commercial Sale of such Reverse Royalty Terminated Territory Product in such Terminated Territory (whether occurring before or after this Section 11.5.3(i) becomes operative).

During such period (if any) as Targacept is required to pay royalties to AstraZeneca pursuant to this Section 11.5.3(i), the definition of "Net Sales," "Net Sales Distributors," and Sections 5.3.1(c)(i-iv), 5.3.1(d), and 5.5 through 5.10 shall apply *mutatis mutandis* to the calculation (including credits and offsets), payment, recording and auditing of Targacept's obligations to pay royalties under this Section 11.5.3(i) as they apply to AstraZeneca and, solely for such purpose, each reference in each such Section (and any related definitions) to AstraZeneca shall be deemed to be a reference to Targacept.

(j) each Party's rights and obligations under Articles 2 and 3, AstraZeneca's obligations under Article 5, and the Parties' representations, warranties and covenants under Article 9 shall survive, but in each case solely with respect to the Territory, and each Party's obligations under Article 6 shall survive. For clarity, AstraZeneca shall have no obligation to make any payment pursuant to Section 5.2 with respect to any Milestone Event that occurs with respect to a Terminated Territory after the effective date of termination of this Agreement with respect to such Terminated Territory; and

(k) each Party's rights and obligations governing ownership, Prosecution and Maintenance, enforcement, and defense of Patent Rights and other intellectual property under Article 7, except as provided in Section 11.5.3(d)(vi), and the Parties' respective confidentiality obligations under Article 8 and indemnification obligations under Article 10 shall survive in their entirety.

11.5.4 In the event of a termination of this Agreement in its entirety by AstraZeneca pursuant to Section 11.2.1 or Section 11.4.1:

(a) the rights and licenses granted to AstraZeneca pursuant to Section 4.1.1 shall survive such termination (for clarity, beyond the end of the Term notwithstanding anything to the contrary in Section 4.1.1) and AstraZeneca shall have the right to grant sublicenses (through multiple tiers) thereunder;

(b) solely if both (i) such termination results from an uncured material breach of a representation or warranty of Targacept in Section 9.2 and (ii) the failure of such representation or warranty to be true constitutes a material change to the ******** of the Primary Compound as compared to the ******** of the Primary Compound if such representation or warranty were true (in each case considered as of the Execution Date with all other factors unchanged), then the royalty rates set forth in Section 5.3.1 and the milestone obligations set forth in Section 5.2 shall be adjusted in an amount to be determined by the Parties to reflect royalty rates and milestone obligations that a pharmaceutical company similarly situated to AstraZeneca would pay and assume for the same rights with respect to a compound with the post-breach ******** of the Primary Compound as AstraZeneca has with respect to the Primary Compound hereunder; provided that, if the Parties cannot agree, each Party may submit the matter for resolution pursuant to 'baseball' arbitration pursuant to Section 12.1.3;

(c) all rights and licenses granted by AstraZeneca pursuant to Section 4.1.2 hereunder shall immediately terminate;

(d) to the extent requested in writing by AstraZeneca, Targacept shall promptly: (i) unless expressly prohibited by any Regulatory Authority, transfer control to AstraZeneca of all Clinical Studies of each Compound or Licensed Product being conducted as of the effective date of termination and continue to conduct such Clinical Studies, at AstraZeneca's cost, for up to ******** to enable such transfer to be completed without interruption of any such Clinical Study; provided that (A) for clarity, AstraZeneca shall not have any obligation to continue any Clinical Study except as required by Applicable Laws and (B) with respect to each Clinical Study for which such transfer is expressly prohibited by the applicable Regulatory Authority, if any, Targacept shall continue to conduct such Clinical Study to completion, at AstraZeneca's reasonable cost; (ii) assign (or cause its Affiliates to assign) to AstraZeneca all agreements with any Third Party with respect to the conduct of Clinical Studies of each Compound or Licensed Product including agreements with contract research organizations, clinical sites and investigators, unless, with respect to any such agreement, such agreement (A) expressly prohibits such assignment, in which case Targacept shall cooperate with AstraZeneca in all reasonable respects to secure the consent of such Third Party to such assignment, or (B) covers clinical trials for Combination Products in which any active pharmaceutical ingredient that is not a Compound is covered by Patent Rights of Targacept or products covered by Patent Rights of Targacept in addition to Licensed Products, in which case, Targacept would be required, at AstraZeneca's sole cost and expense, to cooperate with AstraZeneca in all reasonable respects to facilitate the execution of a new agreement between AstraZeneca and the applicable Third Party; and (iii) subject to any Third Party agreement, provide AstraZeneca with copies of all reports and data generated or obtained by Targacept or any of its Affiliates that relate to any Compound or Licensed Product that have not previously been provided to AstraZeneca; and

(e) subject to clause (b) above, if applicable, the rights and obligations of the Parties under Article 5 shall survive.

11.6 **Return of Confidential Information**. In the event of termination of this Agreement, each Party shall return all data, files, records and other materials in its possession or control containing or comprising the other Party's Confidential Information (in the event of termination of this Agreement with respect to one or more Terminated Territories but not in its entirety, solely to the extent relating to such Terminated Territories but not the Territory) to which such first Party does not retain rights under the surviving provisions of this Agreement (except one copy of which may be retained solely for archival purposes). Upon the effective date of such termination, Targacept Licensed Product Information that AstraZeneca is required to return pursuant to the immediately preceding sentence shall be deemed Confidential Information only of Targacept. For clarity, in the event of termination of this Agreement with respect to any Terminated Territory (but not in its entirety), AstraZeneca shall have the right to retain a copy of all such Confidential Information that is necessary or reasonably useful for AstraZeneca to Develop and Commercialize Compound or Licensed Products with respect to the Territory.

11.7 **Accrued Rights; Surviving Provisions**.

11.7.1 *Accrued Rights.* Expiration or termination of this Agreement shall be without prejudice to any rights or remedies that have accrued hereunder to the benefit of a Party prior to such expiration or termination or that either Party may otherwise have at law or in equity. In addition, such expiration or termination shall not relieve either Party from obligations that are expressly indicated to survive expiration or termination of this Agreement.

11.7.2 *Surviving Provisions.* In addition to the provisions of this Agreement that survive termination of this Agreement pursuant to any provision of this Agreement, the provisions of Sections 3.7.1(c), 3.7.3(c), 3.9.2(a), 3.9.2(b), 3.11.2 (last sentence only), 4.1.4, 4.2, 5.5, 5.6, 5.7, 6.1.3, 6.2.1, 6.2.2, 6.2.3, 6.2.4, 7.1, 7.2, 7.3, 7.10, 7.11, 7.14, 8.1, 8.2, 8.3, 8.4, 12.1, 12.2, 12.3, 12.4 (excluding Section 12.4.1), 12.6, 12.7, 12.8, 12.9, 12.10, 12.11, 12.12, 12.13, 12.14, 12.15, 12.16 and 12.17, and Articles 10 and 11 (including, for purposes of Section 11.5.1(f) and Section 11.5.3(c)(i), Sections 5.3.1(c)(i-iv), 5.3.1(d) and 5.5 through 5.10), shall survive expiration or termination of this Agreement (including, for purposes of interpreting any such Section or Article, Article 1 and all Sections, Articles or Schedules referenced in any such Section or Article).

ARTICLE 12
MISCELLANEOUS

12.1 **Dispute Resolution**.

12.1.1 Except as provided in Section 2.1.5 or Section 12.4 and except with respect to any provision of this Agreement that provides for a different dispute resolution mechanism in a particular context, in the event of any dispute concerning the validity, interpretation or construction of, compliance with, or breach of, this Agreement (each, a "**Dispute**"), either Party may, by written notice to the other Party, have such dispute referred to their respective Executive Officers for attempted resolution by good faith negotiations within ******** days after such notice is received. In the event the Executive Officers are not able to resolve such dispute within such ******** day period, then, either Party may submit such Dispute to arbitration pursuant to Section 12.1.2.

12.1.2 *Binding Arbitration*. The arbitration proceeding shall be conducted in accordance with the Commercial Arbitration Rules and Supplementary Procedures for Large Complex Disputes of the AAA and otherwise as described in this Section 12.1.2.

(a) The arbitration shall be conducted by a panel of three (3) persons who have sufficient background and experience in pharmaceutical development or commercialization, as applicable, to resolve the Dispute and are independent of both Parties and conflict-free (the "**Experts**"); provided that the Parties may instead by mutual agreement select a single independent, conflict-free Expert. Subject to the foregoing proviso, within ******** days after initiation of arbitration, each Party shall select one person to act as an Expert and the two (2) Party-selected Experts shall select a third Expert within ******** days of their appointment. If the Experts selected by the Parties are unable or fail to agree upon the third Expert, the third Expert shall be appointed by the AAA of Washington D.C. The place of arbitration shall be Washington, D.C., and all proceedings and communications shall be in English.

(b) The Expert(s) shall make a final decision with respect to the Dispute within ******** days following the arbitration proceeding; provided that the Expert(s) shall have no authority to award punitive or any other type of damages not measured by a Party's compensatory damages.

(c) Either Party may apply to the Expert(s) for interim injunctive relief until the arbitration decision is rendered or the Dispute is otherwise resolved. Either Party also may, without waiving any right or remedy under this Agreement, seek from any court having jurisdiction any injunctive or provisional relief necessary to protect the rights or property of that Party pending resolution of the Dispute pursuant to this Section 12.1.2. Each Party shall bear its own costs and expenses and attorneys' fees, and the Party that does not prevail in the arbitration proceeding shall pay the Experts' fees and any administrative fees of arbitration.

(d) Except to the extent necessary to confirm an award or decision or as may be required by Applicable Laws, neither Party may, and the Parties shall instruct the Expert(s) not to, disclose the existence, content, or results of an arbitration without the prior written consent of both Parties. In no event shall an arbitration be initiated after the date when commencement of a legal or equitable proceeding based on the Dispute would be barred by the applicable New York statute of limitations.

(e) The Parties hereby agree that any payment to be made by a Party pursuant to a decision of the Expert(s) shall be made in Dollars.

(f) The decision of the Expert(s) shall be the sole, exclusive and binding remedy between the Parties regarding determination of each Dispute presented.

12.1.3 *Baseball Arbitration*. Under the circumstances described in Section 3.10.4 or Section 11.5.4(b), either Party may elect to have the matter resolved by expedited arbitration by an Expert. The arbitration proceeding shall be conducted in accordance with the Commercial Arbitration Rules of the AAA and otherwise as described in this Section 12.1.3. Upon written request by either Party to the other Party, the Parties shall promptly negotiate in good faith to appoint an appropriate Expert. If the Parties are not able to agree within ******** days after the receipt by a Party of the written request in the immediately preceding sentence, the AAA of Washington D.C, or such other similar entity as the Parties may agree, shall be responsible for selecting an Expert with background and experience in pharmaceutical commercialization within ******** days of being approached by a Party. The fees and costs of the Expert and the AAA (or such other entity) shall be shared equally (50%/50%) by the Parties. Within ******** days after the designation of the Expert, the Parties shall each simultaneously submit to the Expert and one another a written statement of their respective positions on such disagreement. Each Party shall have ******** Business Days from receipt of the other Party's submission to submit a written response thereto. The Expert shall have the right to meet with the Parties, either alone or together, as necessary to make a determination. Further, the Expert shall have the right to request information and materials and to require and facilitate discovery as it shall determine is appropriate in the circumstances, taking into account the needs of the Parties and the desirability of making discovery expeditious and cost-effective determinations. No later than ******** days after the designation of the Expert, or as otherwise agreed by the Parties, the Expert shall make a determination by selecting the resolution proposed by one of the Parties that as a whole is the most consistent with this Agreement and the most fair and reasonable to the Parties in light of the totality of the circumstances. The Expert shall provide the Parties with a written statement setting forth the basis of the determination in connection therewith. The decision of the Expert shall be final, binding and conclusive, absent manifest error.

12.2 **Notices**. All notices and communications shall be in writing and delivered personally, by facsimile transmission, or by internationally-recognized overnight express courier providing evidence of delivery or mailed via certified mail, return receipt requested, addressed as follows, or to such other address as may be designated from time to time:

If to AstraZeneca:

AstraZeneca AB
V-Malarehamnen 9
S-151 85 Södertälje
Sweden
Tel: 46 8 553 260 00
Fax: 46 8 553 288 12
Attention: Secretary

With a copy to:

AstraZeneca UK Ltd.
G37 Alderley House
Alderley Park
Macclesfield, Cheshire
England
SK10 4TF
Tel: 44 (0)1625 515802
Fax: 44 (0)1625 518805
Attention: Deputy General Counsel - Corporate

If to Targacept:

Targacept, Inc.
200 East First Street
Suite 300
Winston-Salem, NC 27101-4165
Tel: (336) 480-2100
Fax: (336) 480-2103
Attention: Chief Executive Officer

With a copy to:

Targacept, Inc.
200 East First Street
Suite 300
Winston-Salem, NC 27101-4165
Tel: (336) 480-2100
Fax: (336) 480-2103
Attention: General Counsel

In addition, all notices to the JDC shall be sent to each Party's designated members of such committees at such Party's address stated above or to such other address as such Party may designate by written notice given in accordance with this Section 12.2; provided that, notwithstanding the foregoing, notices to each member of the JDC may be sent by email to a known email address of the recipient.

Except as otherwise expressly provided in this Agreement or mutually agreed in writing, any notice, communication or document (excluding payment) required to be given or made shall be deemed given or made and effective upon actual receipt or, if earlier, (a) ******** Business Days after deposit with an internationally-recognized overnight express courier with charges prepaid (b) ******** Business Days after mailed by certified, registered or regular mail, postage prepaid, or (c) the date transmitted by facsimile (with transmission confirmed), in each case (clauses (a), (b) and (c)) addressed to a Party at its address stated above or to such other address as such Party may designate by written notice given in accordance with this Section 12.2. Any notice delivered by facsimile shall be confirmed by a copy delivered by courier or mail as provided above as soon as practicable thereafter.

12.3 **Governing Law**. This Agreement shall be governed by and construed in accordance with the laws of the State of New York (U.S.A.), excluding any conflicts or choice of law rule or principle that might otherwise refer construction or interpretation of this Agreement to the substantive law of another jurisdiction.

12.4 **Equitable Relief**. Each Party acknowledges and agrees that the restrictions set forth in Section 6.1 and Article 8 of this Agreement are reasonable and necessary to protect the legitimate interests of the other Party and that the other Party would not have entered into this Agreement in the absence of such restrictions.

12.4.1 *Section 6.1*. Each Party acknowledges and agrees that any breach or threatened breach of Section 6.1 would result in irreparable injury to the other Party for which there will be no adequate remedy at law. In the event of a breach or threatened breach of Section 6.1 by a Party, the other Party shall be authorized and entitled to obtain from any court of competent jurisdiction equitable relief, whether preliminary or permanent, specific performance and an equitable accounting of all earnings, profits and other benefits arising from such breach, which rights shall be cumulative and in addition to any other rights or remedies to which the Party may be entitled in law or equity. Each Party agrees (a) to waive any requirement that the other Party post a bond or other security as a condition for obtaining any such relief and (b) to waive any requirement that the other Party show irreparable harm, balancing of harms, consideration of the public interest or inadequacy of monetary damages as a remedy.

12.4.2 *Article 8*. Each Party acknowledges and agrees that any breach or threatened breach of Article 8 might result in irreparable injury to the other Party for which there might be no adequate remedy at law. In the event of a breach or threatened breach of Article 8 by a Party, the other Party shall be entitled to seek to obtain from any court of competent jurisdiction equitable relief, whether preliminary or permanent, specific performance and an equitable accounting of all earnings, profits and other benefits arising from such breach, which rights, if granted, would be cumulative and in addition to any other rights or remedies to which the Party may be entitled in law or equity.

12.4.3 *Other*. Nothing in this Section 12.4 is intended, or should be construed, to limit either Party's rights to equitable relief or any other remedy for a breach of any provision of this Agreement besides Section 6.1 or Article 8.

12.5 **Targacept Change of Control**.

12.5.1 *Notice*. If Targacept enters into an agreement that results or, if the transaction contemplated thereby is completed, would result, in a Change of Control of Targacept, Targacept shall provide AstraZeneca with prompt written notice describing such Change of Control in reasonable detail (the "**Targacept Change of Control Notice**"). The Targacept Change of Control Notice shall be provided by Targacept promptly following the earlier of (a) the public disclosure of the entry into such agreement and (b) consummation of the transaction constituting the Change of Control.

12.5.2 *Consequences of Change of Control of Targacept*. Upon the occurrence of any Change of Control of Targacept:

(a) AstraZeneca shall have the option to disband the JDC and any or all Working Groups by giving written notice to Targacept within ************ after the later of the date the Targacept Change of Control Notice is delivered to AstraZeneca and the consummation of the Change of Control transaction (the "**Election Period**"), and if AstraZeneca elects to disband the JDC or any Working Group any activities and decisions that would otherwise have been performed, made or subject to determination by the JDC or such Working Group, as the case may be, shall be performed, made or determined by AstraZeneca acting unilaterally;

(b) AstraZeneca may elect, by delivering written notice to Targacept within the Election Period, to terminate the Parties' right to appoint Alliance Mangers and Development Liaisons;

(c) AstraZeneca may elect, by delivering written notice to Targacept within the Election Period, to terminate Targacept's rights under Section ********;

(d) AstraZeneca may elect, by delivering written notice to Targacept within the Election Period, to terminate Targacept's Co-Promotion Right and the Co-Promotion Agreement (if any) and Targacept's rights under Sections ******** and ********; and

(e) AstraZeneca shall have no obligations to provide ******** or ********, or to ******** with respect to the Development and Commercialization of Compounds or Licensed Products under this Agreement, except to: (i) provide ******** as provided in Section ******** and ******** as provided in Section ******** and (ii) comply with the audit requirements provided in Section 5.5.

12.6 **Binding Effect**. This Agreement shall be binding upon and inure to the benefit of the Parties and their respective legal representatives, successors and permitted assigns.

12.7 **Headings**. Section and subsection headings are inserted for convenience of reference only and do not form a part of this Agreement.

12.8 **Counterparts**. This Agreement may be executed simultaneously in two (2) or more counterparts, each of which shall be deemed an original and all of which, together, shall constitute a single agreement. An executed signature page of this Agreement delivered by facsimile transmission or in PDF format via email shall be as effective as the manual exchange of an originally executed signature page.

12.9 **Amendment; Waiver**. This Agreement may be amended, modified, superseded or canceled, and any of the terms of this Agreement may be waived, only by a written instrument executed by each Party or, in the case of waiver, by the Party or Parties waiving compliance. The delay or failure of either Party at any time or times to require performance of any provision shall in no manner affect the rights at a later time to enforce the same. No waiver by either Party of any condition or of the breach of any term contained in this Agreement, whether by conduct, or otherwise, in any one or more instances, shall be deemed to be, or considered as, a further or continuing waiver of any such condition or of the breach of such term or any other term of this Agreement.

12.10 **No Third Party Beneficiaries**. Except as set forth in Section 7.7.6, no Third Party (including no employee of either Party) shall have or acquire any rights by reason of this Agreement.

12.11 **Purposes and Scope**. The Parties understand and agree that this Collaboration is limited to the activities, rights and obligations as set forth in this Agreement and the relationship between the Parties is that of independent contractors. Nothing in this Agreement shall be construed to: (a) create or imply a general partnership or joint venture between the Parties; (b) make either Party the agent of the other for any purpose; (c) to alter, amend or supersede any other arrangements between the Parties with respect to any subject matters not covered hereunder; (d) to give either Party the right to bind the other; (e) to create any duties or obligations between the Parties except as expressly set forth herein; or (f) to grant any direct or implied licenses or any other right other than as expressly set forth herein.

12.12 **Assignment and Successors**. Neither Party shall assign its rights or, subject to Section 3.12, delegate its obligations under this Agreement without the consent of the other, which shall not be unreasonably withheld, conditioned or delayed, except that: (a) each Party may assign this Agreement and the rights, obligations and interests of such Party (i) in whole or in part, to any of its Affiliates or (ii) in whole, but not in part, to any purchaser of all or substantially all of its assets to which this Agreement relates or to any successor resulting from a Change of Control; and (b) each Party shall always have the right to perform any or all of its obligations and exercise any or all of its rights under this Agreement through any of its Affiliates, but, in such event, shall remain responsible for and liable with respect to such obligations.

12.13 **Force Majeure**. Neither AstraZeneca nor Targacept shall be liable for failure of or delay in performing obligations set forth in this Agreement, and neither shall be deemed in breach of its obligations, if such failure or delay is due to a Force Majeure. In event of such Force Majeure, the Party affected shall use diligent efforts to cure or overcome the same and resume performance of its obligations hereunder.

12.14 **Export Control**. This Agreement is made subject to any restrictions concerning the export of products or technical information from the U.S. Territory or other countries that may be imposed on the Parties from time to time. Each Party agrees that it will not export, directly or indirectly, any technical information acquired from the other Party under this Agreement or any products using such technical information to a location or in a manner that at the time of export requires an export license or other governmental approval, without first obtaining the written consent to do so from the appropriate agency or other governmental authority in accordance with applicable law.

12.15 **Interpretation**. The Parties hereto acknowledge and agree that: (a) each Party and its counsel reviewed and negotiated the terms and provisions of this Agreement and have contributed to its revision; (b) the rule of construction to the effect that any ambiguities are resolved against the drafting Party shall not be employed in the interpretation of this Agreement; and (c) the terms and provisions of this Agreement shall be construed fairly as to each Party and not in a favor of or against either Party, regardless of which Party was generally responsible for the preparation of this Agreement. In addition, unless a context otherwise requires, wherever used in this Agreement (including any Schedule hereto): (i) the singular shall include the plural and the plural shall include the singular; (ii) the use of any gender shall be applicable to all genders; the word "or" is used in the inclusive sense (and/or); (iii) the words "including," "taking into account" and all correlative words are used without limitation and shall mean "including without limitation," "taking into account without limitation" or their respective correlative words, as the case may be; (iv) any statutory or regulatory citation includes such statute or regulation as amended or as superseded by any other statute or regulation; (v) consistent with the absence of any duty to conduct any investigation with respect to the applicable facts or information by reason of the execution of this Agreement or the formation of the Collaboration, no statement, representation or warranty made or given to the Knowledge of a Party shall create any implication that, be construed to mean that or constitute a certification, representation or warranty that any one or more of the individuals identified (by name or position) in clause (a) or clause (b) of the definition of "Knowledge" knows affirmatively (i.e., so as to be able to positively confirm) such facts and information to be true and correct, and each such statement, representation or warranty shall constitute negative assurance as to such facts and information; (vi) all references to a Party's Controlling Affiliate shall be if any; and (vii) all references to JDC approval or a JDC determination shall be subject to resolution in accordance with Section 2.1.5.

12.16 **Integration; Severability**. This Agreement sets forth the entire agreement with respect to the subject matter hereof and supersedes all other agreements and understandings between the Parties or their Affiliates with respect to such subject matter, including the Existing CDA. To the fullest extent permitted by Applicable Law, the Parties waive any provision of law that would render any provision in this Agreement invalid, illegal or unenforceable in any respect. If any provision of this Agreement is held to be invalid, illegal or unenforceable, in any respect, then such provision will be given no effect by the Parties and shall not form part of this Agreement. To the fullest extent permitted by Applicable Laws and if the rights or obligations of either Party, taken as a whole, will not be materially and adversely affected, all other provisions of this Agreement shall remain in full force and effect, and the Parties shall use their best efforts to negotiate a provision in replacement of the provision held invalid, illegal or unenforceable that is consistent with Applicable Laws and achieves, as nearly as possible, the original intention of the Parties.

12.17 **Further Assurances**. Each of Targacept and AstraZeneca agrees to duly execute and deliver, or cause to be duly executed and delivered, such further instruments and do and cause to be done such further acts and things, including the filing of such additional assignments, agreements, documents and instruments, as the other Party may at any time and from time to time reasonably request in connection with this Agreement or to carry out more effectively the provisions and purposes of, or to better assure and confirm unto such other Party its rights and remedies under, this Agreement.

12.18 **HSR Filing**. Each Party shall, as promptly as practicable after the Execution Date, file or cause to be filed with the U.S. Federal Trade Commission and the U.S. Department of Justice and any relevant foreign governmental authority any notifications required to be filed under the HSR Act with respect to the transactions contemplated hereby; provided that the Parties shall each file the notifications required to be filed under the HSR Act within ******** Business Days after the Execution Date. The Parties shall cooperate with each other in the preparation of any such filing. The Parties shall use diligent efforts to respond promptly to any requests for additional information made by either of such agencies and to cause the waiting period (and any extension thereof) under the HSR Act to terminate or expire at the earliest possible date after the date of filing. If the Parties have failed to obtain the necessary clearances required under the HSR Act by March 1, 2010, either Party shall have the right, on written notice to the other Party, to terminate this Agreement. Each Party shall bear all costs and expenses incurred by it in connection with filings under the HSR Act, except that AstraZeneca shall be responsible for the filing fees associated with such filings by either Party.

12.19 **Prior to Effective Date**.

12.19.1 Targacept shall conduct its business with respect to the Primary Compound and Licensed Products in the ordinary course, consistent with past practices, during the period from the Execution Date until the earlier of (a) Effective Date or (b) **********, 2010, including by not conducting any End of Phase 2 Meeting with the FDA relating to any Licensed Product or initiating any Phase 3 Clinical Trial for any Licensed Product. For clarity, the submission by Targacept of documents, questions or other information or materials to, or other communication with, the FDA in contemplation of an End of Phase 2 Meeting to be conducted after the earlier of the Effective Date or **********, 2010 is expressly permitted and shall not be deemed to violate or breach this Section 12.19.1 or any other provision of this Agreement.

12.19.2 Notwithstanding anything in this Agreement to the contrary, (a) neither Party shall have the right to amend, modify or update in any respect the Amplixa Global Development Outline or the first Amplixa Annual Global Development Plan during the period from the Execution Date until the Effective Date and (b) any such amendment, modification or update made by a Party notwithstanding this Section 12.19.2 shall be null and void and of no force or effect.

12.19.3 Notwithstanding anything in this Agreement to the contrary, this Agreement (other than Section 8.4, Section 12.18 and this Section 12.19)) shall not become effective unless and until the waiting period (or any extension thereof) under the HSR Act in the United States has expired or been terminated early (the date of such expiration or earlier termination, the "**Effective Date**").

12.19.4 Each Party shall use diligent efforts to ensure that its representations and warranties set forth in this Agreement remain true and correct at and as of the Effective Date as if such representations and warranties were made at and as of the Effective Date.

*** - * - * - ***

[remainder of page intentionally left blank]

IN WITNESS WHEREOF, the Parties have caused this Agreement to be executed by their duly authorized representatives as of the Execution Date.

TARGACEPT, INC.

By: /s/ J. Donald deBethizy
Name: J. Donald deBethizy
Title: President & Chief Executive Officer

ASTRAZENECA AB (publ)

By: /s/ Anders Ekblom
Name: Anders Ekblom
Title: Authorised Signatory

SCHEDULE 1

DESCRIPTION OF THE PRIMARY COMPOUND

Chemical IUPAC Name:

****

Structural Formula:

****

SCHEDULE 2

EXISTING PATENT RIGHTS

Part A: Owned Patent Rights

Country	Filing Date	Application #	Issue Date	Pat#
*********				
*********				
*********				
*********				
*********				
*********				
*********				
*********				
*********				
*********				
*********				
*********				

Part B: In-Licensed Patent Rights

Country	Filing Date	Application #	Issue Date	Pat#
*********				
*********				
US	6/15/01	09/882,935	5/11/04	6,734,215
US	5/19/03	10/441,947	9/5/06	7,101,916
*********				
*********				
*********				
Europe	12/16/99	99967401.3	3/22/06	1,139,743
Austria		99967401.3		1,139,743
Belgium		99967401.3		1,139,743
Switzerland		99967401.3		1,139,743
Germany		99967401.3		69930552.7-08
Denmark		99967401.3		1,139,743
Spain		99967401.3		1,139,743
Finland		99967401.3		1,139,743
France		99967401.3		1,139,743
UK		99967401.3		1,139,743
Greece		99967401.3		20060401770
Ireland		99967401.3		1,139,743
Italy		99967401.3		1,139,743
Luxembourg		99967401.3		1,139,743
Netherlands		99967401.3		1,139,743
Portugal		99967401.3		1,139,743
Sweden		99967401.3		1,139,743
Europe div.	12/16/99	5024899.6	9/3/08	1,634,498
Austria		5024899.6		1,634,498
Belgium		5024899.6		1,634,498
Switzerland		5024899.6		1,634,498
Cyprus		5024899.6		1,634,498
Germany		5024899.6		69939498.8-08
Denmark		5024899.6		1,634,498
Spain		5024899.6		1,634,498
Finland		5024899.6		1,634,498
France		5024899.6		1,634,498
UK		5024899.6		1,634,498
Greece		5024899.6		20080403093
Ireland		5024899.6		1,634,498
Italy		5024899.6		1,634,498
Luxembourg		5024899.6		1,634,498
Monaco		5024899.6		1,634,498
Netherlands		5024899.6		1,634,498
Portugal		5024899.6		1,634,498
Sweden		5024899.6		1,634,498
*********				
*********				
*********				
US	11/23/98	09/198,882	3/7/00	6,034,079
US	3/15/00	09/526,403	12/27/05	6,979,698
*********				
Canada	8/11/98	2,300,148	6/23/09	2,300,148
Europe	8/11/98	98939328.5	12/19/07	1,011,678
Austria		98939328.5		1,011,678
Belgium		98939328.5		1,011,678
Switzerland		98939328.5		1,011,678

Cyprus		98939328.5		1,011,678
Germany		98939328.5		69838875.5-08
Denmark		98939328.5		1,011,678
Spain		98939328.5		1,011,678
Finland		98939328.5		1,011,678
France		98939328.5		1,011,678
UK		98939328.5		1,011,678
Greece		98939328.5		20080400416
Ireland		98939328.5		1,011,678
Italy		98939328.5		1,011,678
Netherlands		98939328.5		1,011,678
Portugal		98939328.5		1,011,678
Sweden		98939328.5		1,011,678
********				
Taiwan	11/4/98	87113218	6/1/05	I-233,354
South Africa	8/11/98	98/7182	8/31/99	98/7182
********				
********				
********				
********				
********				

Part C: ****** Application**

****
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SCHEDULE 3

EXISTING TRADEMARKS

AMPLIXA	Canada	Filed
AMPLIXA	Community Trademark	Registered
AMPLIXA	Japan	Registered
AMPLIXA	Mexico	Filed
AMPLIXA	United States	Filed (2)
INVERSINE	Ireland	Registered
INVERSINE (block letters)	United States	Registered
INVERSINE (stylized)	United States	Registered

amplixa.com
amplixa.net
amplixa.org
amplixa.us
inversine.com
inversine.net
inversine.org
mecamylamine.com
mecamylamine.net
mecamylamine.org

SCHEDULE 4

SPECIAL MILESTONE CRITERIA

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SCHEDULE 5

FORM OF ASSIGNMENT AND ASSUMPTION AGREEMENT

ASSIGNMENT AND ASSUMPTION AGREEMENT

This **ASSIGNMENT AND ASSUMPTION AGREEMENT** (this "**Agreement**") is entered into as of the 15th day of January 2010 (the "**Effective Date**") by and between Targacept, Inc., a Delaware corporation having its principal place of business at 200 East First Street, Winston-Salem, North Carolina 27101 ("**Targacept**"), and AstraZeneca AB, a company limited by shares organized and existing under the laws of Sweden having a principal place of business at V-Malarehamnen 9, S-151 85 Södertälje, Sweden ("**AstraZeneca**"). Targacept and AstraZeneca are each referred to herein by name or as a "**Party**" or, collectively, as the "**Parties**." All capitalized terms used but not defined herein shall have the meanings set forth in that certain Collaboration and License Agreement by and between the Parties dated as of December 3, 2009 (the "**Collaboration Agreement**").

RECITALS

WHEREAS, Targacept is a party to (a) that certain Amended and Restated Supply Agreement by and among Targacept, Poli Industria Chimica, SpA ("**Poli**") and Interchem Corporation ("**Interchem**") dated December 3, 2009, attached hereto as Annex A (the "**Existing TRGT Supply Agreement**"), the related Quality Agreement by and among Targacept, Poli and Interchem dated December 3, 2009, attached hereto as Annex B (the "**Existing TRGT Quality Agreement**"), and the related Services Agreement by and among Targacept, Poli and Interchem dated July 28, 2006, as amended, attached hereto as Annex C (the "**Existing TRGT Services Agreement**" and, together with the Existing TRGT Supply Agreement and the Existing TRGT Quality Agreement, the "**Existing TRGT API Agreements**"), and (b) that certain Master Services Agreement by and between Targacept and ************ dated August 13, 2009, and Work Order No. 1 dated August 13, 2009 thereunder, attached hereto as Annex D (collectively, the "********** Agreement**" and, together with the Existing TRGT API Agreements, the "**Manufacturing Agreements**");

WHEREAS, the Parties have entered into the Collaboration Agreement, pursuant to which the Parties established a worldwide, strategic collaboration for the continued development of the Primary Compound, and potentially for the development of other Compounds, and, if successful, Marketing Approval and Commercialization for Licensed Products; and

WHEREAS, as contemplated by the Collaboration Agreement, Targacept now desires to assign to AstraZeneca the Manufacturing Agreements and AstraZeneca now desires to assume the Manufacturing Agreements, all on the terms set forth herein.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the Parties hereby agree as follows:

ARTICLE 1
ASSIGNMENT AND ASSUMPTION

1.1 Assignment. Targacept hereby assigns, sells, transfers and sets over to AstraZeneca all of Targacept's rights and Liabilities (as defined herein) under the Manufacturing Agreements as of the Effective Date, but expressly excluding any and all Excluded Liabilities (as defined herein). Targacept shall retain and remain solely responsible for, and shall satisfy, perform, pay and discharge when and as due any and all Excluded Liabilities. "**Liability**" means any debt, liability, loss, damage, cost, expense and obligation of any kind (whether fixed or contingent, known or unknown, asserted or unasserted, absolute or contingent, accrued or unaccrued, liquidated or unliquidated, or due or to become due), including any liability for taxes. "**Excluded Liabilities**" means all Liabilities under the Manufacturing Agreements arising, or attributable to actions or omissions occurring, prior to the Effective Date, including Liabilities with respect to any claim or action asserted on or after the Effective Date to the extent the conduct giving rise to such claim or action occurred prior to the Effective Date.

1.2 Acceptance and Assumption. AstraZeneca hereby accepts the assignment made by Targacept herein and hereby assumes and agrees to satisfy, perform, pay and discharge when and as due any and all Liabilities under the Manufacturing Agreements other than the Excluded Liabilities.

ARTICLE 2
GENERAL PROVISIONS

2.1 Entire Agreement. The Parties have entered into the Collaboration Agreement, which contains certain financial and other provisions. This Agreement does not amend, limit or otherwise qualify any representation, warranty, covenant, right or obligation of Targacept or AstraZeneca under the Collaboration Agreement. To the extent there is a conflict between the terms and conditions of this Agreement and the terms and conditions of the Collaboration Agreement, the terms and conditions of the Collaboration Agreement shall govern. Subject to the foregoing, this Agreement (and all Annexes attached hereto) sets forth the entire agreement between the Parties with respect to the subject matter hereof and supersedes all prior discussions and agreements between the Parties with respect to the subject matter hereof.

2.2 Binding Effect. This Agreement shall be binding upon and inure to the benefit of the Parties and their respective legal representatives, successors and permitted assigns.

2.3 Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of New York (U.S.A.), excluding any conflicts or choice of law rule or principle that might otherwise refer construction or interpretation of this Agreement to the substantive law of another jurisdiction.

2.4 Headings. Section and subsection headings are inserted for convenience of reference only and do not form a part of this Agreement.

2.5 Counterparts. This Agreement may be executed simultaneously in two (2) or more counterparts, each of which shall be deemed an original and all of which, together, shall constitute a single agreement. An executed signature page of this Agreement delivered by facsimile transmission or in PDF format via email shall be as effective as the manual exchange of an originally executed signature page.

2.6 Amendment; Waiver. This Agreement may be amended, modified, superseded or canceled, and any of the terms of this Agreement may be waived, only by a written instrument executed by each Party or, in the case of waiver, by the Party or Parties waiving compliance. The delay or failure of either Party at any time or times to require performance of any provision shall in no manner affect the rights at a later time to enforce the same. No waiver by either Party of any condition or of the breach of any term contained in this Agreement, whether by conduct, or otherwise, in any one or more instances, shall be deemed to be, or considered as, a further or continuing waiver of any such condition or of the breach of such term or any other term of this Agreement.

2.7 No Third Party Beneficiaries. No Third Party (including no employee of either Party), shall have or acquire any rights by reason of this Agreement.

2.8 Interpretation. The Parties hereto acknowledge and agree that: (a) each Party and its counsel reviewed and negotiated the terms and provisions of this Agreement and have contributed to its revision; (b) the rule of construction to the effect that any ambiguities are resolved against the drafting Party shall not be employed in the interpretation of this Agreement; and (c) the terms and provisions of this Agreement shall be construed fairly as to each Party and not in a favor of or against either Party, regardless of which Party was generally responsible for the preparation of this Agreement. In addition, unless a context otherwise requires, wherever used in this Agreement, the singular shall include the plural, the plural the singular, the use of any gender shall be applicable to all genders, the word “or” is used in the inclusive sense (and/or) and the words “including” and all correlative words are used without limitation and shall mean “including without limitation” or their correlative words, as the case may be.

2.9 Severability. To the fullest extent permitted by Applicable Laws, the Parties waive any provision of law that would render any provision in this Agreement invalid, illegal or unenforceable in any respect. If any provision of this Agreement is held to be invalid, illegal or unenforceable, in any respect, then such provision will be given no effect by the Parties and shall not form part of this Agreement. To the fullest extent permitted by Applicable Laws and if the rights or obligations of either Party, taken as a whole, will not be materially and adversely affected, all other provisions of this Agreement shall remain in full force and effect, and the Parties shall use their best efforts to negotiate a provision in replacement of the provision held invalid, illegal or unenforceable that is consistent with Applicable Laws and achieves, as nearly as possible, the original intention of the Parties.

2.10 Further Assurances. Targacept shall from time to time, at the request of AstraZeneca, execute and deliver, or cause to be executed and delivered, such other documents or instruments of assignment, transfer and conveyance and take such other actions as AstraZeneca may reasonably request, in order to carry out the provisions of this Agreement or more effectively consummate the transactions contemplated hereby.

SIGNATURE PAGE FOLLOWS

IN WITNESS WHEREOF, the Parties have caused this Agreement to be executed by their duly authorized representatives as of the Effective Date.

TARGACEPT, INC.

By: _____

Name: _____

Title: _____

ASTRAZENECA AB (publ)

By: _____

Name: _____

Title: _____

ANNEX A

EXISTING TRGT SUPPLY AGREEMENT

ANNEX B

EXISTING TRGT QUALITY AGREEMENT

ANNEX C

EXISTING TRGT SERVICES AGREEMENT

ANNEX D

********* AGREEMENT**

SCHEDULE 6

MATERIAL TERMS TO BE INCLUDED IN THE CO-PROMOTION AGREEMENT

The Co-Promotion Agreement to be negotiated by the Parties pursuant to Section 3.10.1 of the Agreement shall contain the following material terms. Capitalized terms used but not defined herein shall have the meanings ascribed thereto in the Agreement.

1. Co-Promotion Rights and Obligations.

(a) Subject to the terms and conditions herein, AstraZeneca shall grant to Targacept the right to Detail (as defined herein) each Co-Promoted Product in the U.S. Territory to ******** (together, the "**Target Audience**") in accordance with the Plans (as defined in Section 11 below); provided, however, that Targacept shall be required to provide ******** sales representatives to Detail Co-Promoted Product(s), unless AstraZeneca shall otherwise consent, and not more than ******** sales representatives to Detail Co-Promoted Product(s), unless Targacept and AstraZeneca shall otherwise consent. "**Detail**" means that part of an in person, face-to-face sales call during which a representative, who has successfully completed the training program described in Section 4(b) with respect to the Co-Promoted Product, makes a full presentation of the Co-Promoted Product to a physician or other medical professional with prescribing authority, in a fair and balanced manner consistent with the requirements of the Co-Promotion Agreement and Applicable Laws. For the avoidance of doubt, the following shall not constitute a Detail: (i) e-details; (ii) presentations made at conventions or to any group of more than ******** prescribers; or (iii) mere delivery of sample forms without discussion with a medical professional about the Co-Promoted Product.

(b) Targacept shall perform its activities under the Co-Promotion Agreement in accordance with (i) the PhRMA Code on Interactions with Healthcare Professionals, (ii) Applicable Laws (iii) AstraZeneca's then-current compliance policies for promoting pharmaceutical products, and (iv) the applicable provisions of any corporate integrity agreement to which AstraZeneca (or its applicable Affiliate) is then subject; provided that, in the case of clauses (iii) and (iv), (A) AstraZeneca has provided copies of such compliance policies or applicable provisions to Targacept and (B) training with respect to such compliance policies or applicable provisions has been included in the training program provided to each of Targacept's Designated Sales Forces as described in Section 4(b).

(c) Targacept may perform some or all of its Detailing obligations under the Co-Promotion Agreement through a contract sales organization ("**CSO**"), at Targacept's sole cost and expense; provided that (i) no permitted use of a CSO by Targacept shall relieve Targacept of any of its obligations under the Co-Promotion Agreement, (ii) the individuals provided by such CSO shall promote products (including the Co-Promoted Product(s)) only pursuant to agreement(s) with Targacept, and (iii) each agreement with a CSO shall be subject to the review and approval of AstraZeneca.

2. Sales Force Composition.

(a) Designated Sales Forces. During the term of the Co-Promotion Agreement ("**Term**"), Targacept shall use the number of sales forces assigned to the promotion of a Co-Promoted Product (each, a "**Designated Sales Force**") as set forth in the applicable Plan then in effect to Detail such Co-Promoted Product, provided that such number of Representatives is consistent with Section 1(a).

(b) Minimum Qualifications. Except as may be set forth to the contrary in the applicable Plan, each of Targacept's sales representatives and sales managers shall (i) have graduated from ******** and (ii) have satisfactorily completed the sales training program specified in Section 4(b). In addition, ******** of Targacept's sales representatives and sales managers engaged in the promotion of a Co-Promoted Product at any time during the Term must have been promoting branded pharmaceutical products in the U.S. Territory for ******** prior to the date that such person commences promoting such Co-Promoted Product.

(c) Turnover and Vacancies. During the Term and after the launch of the first Co-Promoted Product in the U.S. Territory, Targacept shall use commercially reasonable efforts to ensure that (i) turnover on any of its Designated Sales Forces in any Calendar Year does not exceed standards customary in the United States contract sales organization industry at the time as reasonably determined by AstraZeneca and set forth in the applicable Plan and (ii) each Designated Sales Force has a maximum vacancy rate for any Calendar Period during the Term that does not exceed standards customary in the United States contract sales organization industry at the time as determined by AstraZeneca and set forth in the applicable Plan.

(d) Sales Force Incentives. The incentive compensation structure for Targacept's Designated Sales Force(s) shall be solely determined by Targacept, provided that each such incentive program shall provide that the weighting for sales performance of the Co-Promoted Product(s) shall be at least ******** of such Targacept's Designated Sales Force(s)' total incentive compensation.

(e) Sales Meetings and Review. Targacept shall permit AstraZeneca's compliance and sales and marketing management personnel (at reasonable levels), upon the request of AstraZeneca, to attend and participate in those portions of its sales meetings that relate solely to the Co-Promoted Product(s); provided that Targacept shall ensure that significant portions of any sales meeting with respect to the Co-Promoted Product(s) shall relate solely to the Co-Promoted Product(s); provided further that ******** shall bear the costs of travel and attendance at such meetings for ******** compliance and sales and marketing management personnel. Further, Targacept shall permit AstraZeneca's compliance and sales and marketing management personnel, upon request of AstraZeneca, to spend time in the field (ride-alongs) with Targacept's sales representatives to assess their performance under the Co-Promotion Agreement (*e.g.*, messaging, quality, sales direction) and compliance with Sections 1(b)(i) – (iv) above.

(f) Non-Solicitation. During the Term and for a period of ******** thereafter, neither Party shall actively recruit or solicit any member of a Designated Sales Force or any other staff of the other Party engaged in the marketing, promotion or Detailing of any Co-Promoted Product. For the avoidance of doubt, this provision shall not restrict either Party or its Affiliates from advertising employment opportunities, engaging head-hunters or engaging in any other activity directed towards recruitment, in each case if and to the extent that such advertising or activities do not directly target the other Party or its Affiliates.

(g) Managed Care. AstraZeneca shall be responsible for managing necessary responsibilities with respect to the Co-Promoted Product(s) across all managed care market segments in the U.S. Territory and shall have exclusive responsibility for: (i) ********, (ii) ********; (iii) ********; (iv) ********; (v) ********; and (vi) all other matters related to managed care.

3. Promotional Materials.

(a) During the Term, AstraZeneca shall create and produce all written, printed or graphic material, other than product labels and inserts, intended for use by sales representatives in promoting Co-Promoted Product(s) in the U.S. Territory, including visual aids, file cards, premium items, clinical study reports, reprints, drug information updates and any other promotional support items (collectively, the "**Promotional Materials**") to be used by the Parties in connection with the co-promotion of Co-Promoted Product(s) in accordance with the terms of the applicable Plan. All Promotional Materials and the directions to sales representatives for the use of such Promotional Materials, in each case provided by AstraZeneca, shall comply with Applicable Laws. The quantities of Promotional Materials for each Co-Promoted Product produced by AstraZeneca (other than materials intended for distribution to patients) shall be allocated to the Parties in proportion to the respective numbers of representatives engaged by the Parties to co-promote such Co-Promoted Product.

(b) Targacept shall, and shall cause its sales representatives to, use only the Promotional Materials provided by AstraZeneca in connection with the promotion of Co-Promoted Product(s). Targacept shall ensure that the Promotional Materials are used only in the form provided and not changed in any way (including by underlining or otherwise highlighting any text or graphics or adding any notes thereto) by any member of its Designated Sales Force(s).

(c) Targacept shall, and shall cause its sales representatives to, immediately cease the use of any Promotional Materials when instructed to do so by AstraZeneca. Targacept shall, and shall cause its sales representatives to, use the Promotional Materials only for the purposes contemplated by the Co-Promotion Agreement. All Promotional Materials in the possession of Targacept or its sales representatives shall be returned to AstraZeneca upon termination of the Co-Promotion Agreement or as earlier requested by AstraZeneca.

(d) Targacept shall, and shall cause its sales representatives to, make only such statements and claims regarding the Co-Promoted Product(s), including as to efficacy and safety, as are consistent with the applicable product labels and inserts and Promotional Materials. Targacept shall not, and Targacept shall cause its sales representatives not to, make any false or misleading statements or comments about the Co-Promoted Product(s).

4. Training.

(a) Training Materials. AstraZeneca shall (i) establish training objectives (including with respect to: disease state; Co-Promoted Product knowledge; competitive product knowledge; compliance with Applicable Law, compliance policies and applicable provisions of any corporate integrity agreement; use of sample forms; reporting of adverse events, field alerts, product quality complaints and PIRs (as defined herein); and other information AstraZeneca deems necessary or appropriate) and training plans for members of Targacept's Designated Sales Force(s) who are hired or assigned to promote Co-Promoted Product(s) and (ii) develop and produce all training programs and materials (including Co-Promoted Product sales orientation assessment tests and refresher tests) to be used by Targacept.

(b) Training Programs. A reasonable time prior to the launch of the first Co-Promoted Product in the U.S. Territory, AstraZeneca, at its expense (including costs for Targacept's representatives travel, food and lodging for training meetings, but excluding Targacept's internal costs for salaries and benefits), shall provide training materials to, and hold in-person meetings or webcasts for, each member of each Targacept's Designated Sales Force prior to his or her commencement of promotion of such Co-Promoted Product to ensure that he or she is appropriately trained in proper Detailing and sales techniques and properly trained and able to satisfy his or her responsibilities under the Co-Promotion Agreement. Following the launch of the first Co-Promoted Product in the U.S. Territory, AstraZeneca shall provide training materials to, and hold in-person meetings or webcasts for, each member of each Targacept's Designated Sales Force as necessary to provide refresher training and training updates. AstraZeneca shall bear the costs of training materials and the costs of its own personnel who provide the refresher training and training updates, and Targacept shall bear all other expenses related to such refresher training and training updates.

5. PDE Requirements. For purposes hereof, "**PDE**" means a primary Detail equivalent where (i) a Primary Product Presentation (a Detail during a sales call in which a Co-Promoted Product ********) has a value of ******** primary Detail equivalent, (ii) a Secondary Product Presentation (a Detail during a sales call in which a Co-Promoted Product ********) has the value of ******** primary Detail equivalents and (iii) a Product Presentation in ********. In any event, no more than three products may be presented during any sales call.

(a) Performance of PDEs. In each calendar trimester, or such other period as AstraZeneca may designate from time to time (each, a "**Calendar Period**"), during the Term, Targacept shall use commercially reasonable efforts to perform the number of PDEs for each Co-Promoted Product to be performed by Targacept as set forth in the applicable Plan for such Calendar Period (the "**Targeted PDEs**"); provided that, without limiting the foregoing, for each Calendar Period, Targacept shall be conclusively presumed to have satisfied such obligation if it performed ******** of the aggregate number PDEs allocated to Targacept in the applicable Plan (consistent with the Section 11) for such Calendar Period. In addition, in each Calendar Period during the Term, Targacept shall ensure that ******** of the number of PDEs it actually performed were made to targeted prescribers. Targacept may deliver ******** of its required PDEs to non-target prescribers if it reasonably believes in good faith that such PDEs are likely to result in increased sales of Co-Promoted Product(s).

(b) Shortfalls. In the event that Targacept believes in good faith that, notwithstanding commercially reasonable efforts, it will be unable to perform the number of Targeted PDEs for any Calendar Period, it shall promptly give written notice to AstraZeneca that it shall not be able to meet its PDE obligations and the projected shortfall in PDEs.

(c) Permissible PDEs. For purposes of determining compliance by Targacept with any of its annual PDE performance requirements set forth in the Co-Promotion Agreement, except as provided in the last sentence of Section 5(a), PDEs that are not performed by Targacept as set forth in the applicable Plan for the applicable Calendar Period, shall not be taken into account.

6. Failure to Perform Required Number of PDEs; Consequences.

(a) Subject to Section 6(c), if, during any ******** Calendar Periods, Targacept fails to perform ******** of its Targeted PDEs for each Co-Promoted Product as set forth in the respective Plans for such Calendar Periods (each such Calendar Period, a "**Shortfall Calendar Period**"), then the PDE Cost (as defined in Section 10) for the Calendar Period immediately following such two Shortfall Calendar Periods (but not any Calendar Period thereafter) shall be equal to the product of (i) ********, (but without regard to this Section 6(a)), multiplied by (ii) ******** such Co-Promoted Product(s) actually performed by Targacept during such ******** Shortfall Calendar Periods, divided by the sum of A + B, where A is ******** of the Targeted PDEs for ******** as set forth in the applicable Plan for such Calendar Period and B is ******** of the Targeted PDEs for ******** as set forth in the applicable Plan for such Calendar Period. The reduction in compensation set forth in this Section 6(a) shall apply whether or not Targacept has used commercially reasonable efforts to perform the Targeted PDEs under the applicable Plans.

(b) Subject to Section 6(c), in addition to any reduction in compensation pursuant to Section 6(a), if during any Calendar Year Targacept performs ******** of the aggregate number of its Targeted PDEs for each Co-Promoted Product to be performed during such Calendar Year as set forth in the applicable Plan for such Calendar Year, then AstraZeneca may terminate the Co-Promotion Agreement by giving notice to Targacept not later ******** days after the end of the Calendar Year during which the termination right arises, and such termination shall become effective ******** days after delivery of such notice. AstraZeneca's right to terminate under this Section 6(b) shall apply whether or not Targacept has used commercially reasonable efforts to perform the Targeted PDEs under the applicable Plan.

(c) Notwithstanding anything herein to the contrary, in no event shall the amount payable to Targacept under the Co-Promotion Agreement be reduced due to a failure of Targacept to provide a particular percentage of Targeted PDEs for particular Calendar Period(s) as set forth in Section 6(a), and in no event shall AstraZeneca have the right to terminate the Co-Promotion Agreement due to a failure of Targacept to provide a particular percentage of Targeted PDEs for particular Calendar Year as set forth in Section 6(b), unless the AstraZeneca field force(s) comparable to Targacept's Designated Sales Force(s) has itself satisfied the same applicable percentage standard, as demonstrated by ******** or ******** to be provided by AstraZeneca to Targacept (in each case generated in a consistent manner).

7. Samples. AstraZeneca may, in its sole and absolute discretion and at its expense, make sample request forms available to Targacept for use by Targacept's sales representatives in Detailing Co-Promoted Product(s). Such sample order forms will be used by Targacept's sales representatives to submit to AstraZeneca requests by prescribers for Co-Promoted Product samples, and AstraZeneca will fulfill such requests by delivering the samples directly to the prescribers. Targacept's sales representatives will not carry any Co-Promoted Product samples. AstraZeneca in its sole and absolute discretion will determine the number of sample request forms (and the number of samples that may be requested pursuant to each such form), if any, to be distributed and sampling strategy for such sample forms.

8. Promotion of Other Products. During the Term, members of each of Targacept's Designated Sales Forces shall be permitted to promote products in addition to Co-Promoted Product(s); provided that such other products have not ********.

9. Reporting and Auditing.

(a) Recordkeeping. Targacept shall keep complete and accurate books and records (financial and otherwise) pertaining to the performance of its obligations under the Co-Promotion Agreement, including records of PDEs performed by its sales representatives, in sufficient detail to calculate all fees and expenses payable pursuant to the Co-Promotion Agreement and to prepare all reports required thereunder. All financial books and records maintained by Targacept shall be maintained in accordance with GAAP.

(b) Detail Reporting. Targacept shall cause each of its sales representatives to report his or her Detailing activity in accordance with the procedures specified from time to time in the applicable Plan. Targacept, at its sole expense, shall ensure that each of its sales representatives on its Designated Sales Force(s) is properly equipped with all necessary hardware, software and other information technology required from time to time by the applicable Plan to perform his or her recordkeeping and reporting obligations under this Section.

(c) Tracking Reports. Targacept shall provide to AstraZeneca such additional information and reports concerning Detail activity under the Co-Promotion Agreement at the times and in the manner specified in the applicable Plan; provided that (i) no less often than ******** during ******** after the launch of each Co-Promoted Product and (ii) no less often than ******** per Calendar Period thereafter, Targacept shall submit to AstraZeneca a written report containing the following information with respect to such ******** or Calendar Period, as the case may be:

(A) the total number of PDEs for such Co-Promoted Product performed by Targacept;

(B) the total number of Primary Product Presentations and Secondary Product Presentations for such Co-Promoted Product performed by Targacept; and

(C) the number of PDEs for such Co-Promoted Product performed by Targacept made in total and individually to target prescribers.

(d) PDE Audits. No more than ******** during any ******** period during the Term, AstraZeneca shall have the right to engage an independent third party auditor (an "**Auditor**") to conduct an audit of Targacept's Detailing activities to confirm the accuracy of the Detail and PDE related-information contained in the reports delivered by Targacept. If the results of such audit identify an overstatement of PDEs, within ******** days after the date on which the Auditor's report is delivered, Targacept shall reimburse the excess payment made by AstraZeneca for such overstated PDEs, with interest at an annual rate of LIBOR plus ******** basis points (or, if less, the maximum interest rate permitted by Applicable Laws) from the date such excess payment was made by AstraZeneca until such excess payment is reimbursed in full by Targacept. Any audit conducted under this Section 9(d) shall be at AstraZeneca's sole expense; provided, however, that if the results of such audit identify an overstatement of PDEs in such reports by ******** more in any Calendar Period, then Targacept shall bear the expense of such audit and shall implement promptly corrective actions reasonably acceptable to AstraZeneca to ensure accurate reporting thereafter. At any time within ******** after the completion of an audit that identifies an overstatement of PDEs by ******** or more in any Calendar Period, AstraZeneca shall have the right to engage an Auditor to conduct, at Targacept's reasonable expense, a subsequent audit of Targacept's Detailing activities, to ensure that Targacept has corrected its reporting deficiencies.

(e) Detail Message Audits. AstraZeneca shall have the right, at its sole expense, to engage an Auditor to conduct market research in order to evaluate the effectiveness of the Details performed by Targacept and the content of the "**Product Message**" (the principal promotional messages with respect to a Co-Promoted Product set forth in the applicable Plan, that a sales representative is required to convey to a prescriber during a Detail of such product) delivered by the Targacept's sales representatives. If such market research indicates that Targacept is not delivering a Product Message consistent with the applicable Plan or the Co-Promotion Agreement, then AstraZeneca may deliver written notice of such failure to Targacept. Within ******** after receipt of such notice, Targacept shall develop and deliver to AstraZeneca a plan of action designed to correct such failure that is reasonably satisfactory to AstraZeneca (a "**Corrective Plan**"). Targacept shall implement the Corrective Plan within ******** after approval thereof by AstraZeneca. AstraZeneca shall have the right, at the reasonable expense of Targacept, to engage an Auditor to conduct independent market research in order to evaluate whether Targacept has corrected such failure in accordance with the Corrective Plan. If such market research indicates that Targacept has not corrected such failure, then AstraZeneca may deliver written notice of such failure to Targacept. Within ******** after receipt of such notice, Targacept (at its sole expense) will develop and deliver to AstraZeneca a comprehensive re-training program for its applicable Designated Sales Force reasonably satisfactory to AstraZeneca (the "**Retraining Program**"), which may utilize the materials developed by AstraZeneca for the training and refresher programs pursuant to Section 4(b). Targacept shall implement the Retraining Program within ********. AstraZeneca shall have the right, at the reasonable expense of Targacept, to engage an Auditor to conduct independent market research in order to evaluate whether Targacept has corrected such failure as a result of the Retraining Program. Without limitation of Section 17(b)(i), if such market research indicates that Targacept has not corrected such failure in one or more sales territories, Targacept will use commercially reasonable efforts to replace within ******** the members of Targacept's Designated Sales Forces Detailing in such sales territories.

10. Co-Promotion Fees and Expenses.

(a) Promotion Fee Payment. Not later than ******** after the end of each Calendar Period during the Term (commencing with the Calendar Period in which the launch of the first Co-Promoted Product in the U.S. Territory occurs), AstraZeneca shall pay to Targacept a fee in an amount equal to (i) the number of PDEs for Co-Promoted Product(s) actually performed by Targacept during such Calendar Period, multiplied by (ii) the PDE Cost applicable for such Calendar Period. In no event shall AstraZeneca pay any compensation to Targacept for PDEs performed by Targacept in any Calendar Period in excess of the Targeted PDEs for such Calendar Period unless AstraZeneca otherwise consents to such excess or to such payment. Except as provided in this Section 10(a), Targacept shall bear and be solely responsible for all costs and expenses incurred by it in the performance of its obligations under the Co-Promotion Agreement.

For purposes hereof, "**PDE Cost**," means (A) with respect to the first ******** period following the launch of the first Co-Promoted Product in the U.S. Territory, the ******** of the good faith quotes obtained jointly by AstraZeneca and Targacept not less than ******** prior to such launch from ******** reputable CSOs in the U.S. Territory for the price that would be charged by such CSOs for performing a PDE on the terms and conditions of the quote specified in the then-current applicable Plan, or, if obtaining such quotes is not reasonably practicable, such other method as may be agreed by the Parties, and (B) with respect to each successive ******** period thereafter, (1) the PDE Cost for the immediately preceding ******** period, multiplied by (2) the sum of ********, rounded to the nearest one Dollar (US $1).

(b) Recruitment Cost Reimbursement. Not later than ******** after the launch of the first Co-Promoted Product in the U.S. Territory, AstraZeneca shall pay Targacept an amount equal to (i) the number of members of Targacept's Designated Sales Force(s) as of such launch date, multiplied by (ii) the ******** of the good faith quotes obtained jointly by AstraZeneca and Targacept not less than ******** prior to such launch from ******** reputable CSOs in the U.S. Territory for the price that would be charged by such CSOs for recruiting a designated sales force.

11. Plan. For each Co-Promoted Product, there shall be a co-promotion plan (each, a "**Plan**") that sets forth, with respect to the applicable annual period, a description of strategy and positioning implementation for such Co-Promoted Product in the U.S. Territory and the key Detailing issues for such Co-Promoted Product in the U.S. Territory including:

(a) a "Promotional Plan" that specifies the Promotional Materials to be used by Targacept in conducting promotional activities with respect to such Co-Promoted Product and the applicable Product Message;

(b) a "Sales Force Management Plan" that specifies, per region or local market within the U.S. Territory, (i) the minimum number of sales representatives and other members of the Designated Sales Force(s) to be provided by Targacept; (ii) the minimum qualifications for sales representatives (to the extent that such minimum represents a change from the minimum set forth in Section 2(b)); (iii) the minimum number of PDEs that each sales representative will perform in each Calendar Period, and (iv) standards for turnover and vacancies for Targacept's Designated Sales Force(s); provided that no such Sales Force Management Plan shall be inconsistent with the proviso in Section 11(c);

(c) a “Strategic Targeting Plan” that specifies Detailing strategy and obligations of Targacept on a Calendar Period basis, including (i) the “call plan” size (i.e., the number of targeted prescribers to be called on by each sales representative); (ii) identification and prioritization of targeted prescribers by deciles; provided that ******** of the total number of PDEs for each Co-Promoted Product allocated to Targacept in each Calendar Period shall be to ******** (substantially comprised of ******** for the Target Indication or, if Regulatory Approval in the U.S. Territory is not obtained for the Target Indication, such other Indication for which such Regulatory Approval is obtained) and the remainder to ******** (substantially comprised of ******** for the Target Indication or, if Regulatory Approval in the U.S. Territory is not obtained for the Target Indication, such other Indication for which such Regulatory Approval is obtained); (iii) reach and frequency expectations for the targeted prescribers in each Calendar Period; and (iv) the number of PDEs for each Co-Promoted Product to be performed in each Calendar Period, which shall equal the product of A x B x C, where A is AstraZeneca’s then-current “Days in Territory” assumption for its full-time specialty care sales representatives that would detail the Co-Promoted Product (“AstraZeneca Sales Force”), B is AstraZeneca’s then-current “Calls Per Day Per Full-Time Specialty Care Sales Representative” assumption for the AstraZeneca Sales Force and C is the number of members of Targacept’s then-current Designated Sales Force(s).

(d) a reporting plan that specifies the reporting obligations of Targacept and its sales representatives with respect to the performance of their promotional activities under the Co-Promotion Agreement, including the recording of Detailing activity by sales representatives; and

(e) such other plans relating to the Detailing and promotion of such Co-Promoted Product in the U.S. Territory as AstraZeneca deems necessary or appropriate; provided that no such plan shall be inconsistent with the proviso in Section 11(c).

Each Plan shall be prepared by AstraZeneca prior to the beginning of the annual period to be covered by any such Plan in accordance with AstraZeneca’s normal procedures with respect to the preparation of promotional plans.

12. Product Supply.

(a) Orders for Products; Terms of Sale. AstraZeneca shall have the sole responsibility and right to fill orders with respect to Co-Promoted Product(s). Targacept shall not take orders for Co-Promoted Product(s), but if for any reason Targacept should receive sales orders for Co-Promoted Product(s), Targacept shall promptly forward such orders to AstraZeneca. All orders for Co-Promoted Product(s) shall be subject to AstraZeneca's acceptance, in its sole discretion. AstraZeneca may cancel any order for Co-Promoted Product(s), or any part thereof, at any time after acceptance without thereby incurring any liability to Targacept. AstraZeneca shall be solely responsible for responding to requests from physicians for individual patients who need the Co-Promoted Product(s) but are unable to afford it. Any such request received by Targacept should be forwarded to AstraZeneca for processing in accordance with AstraZeneca's procedures. AstraZeneca shall have the sole right and responsibility for establishing and modifying the terms and conditions of the sale of Co-Promoted Product(s), including the price at which each Co-Promoted Product will be sold, whether each Co-Promoted Product will be subject to any trade or quantity discounts, whether any discount will be provided for payments on accounts receivable, whether each Co-Promoted Product will be subject to rebates, returns and allowances or retroactive price reductions, the channels of distribution of each Co-Promoted Product, and whether credit is to be granted or refused in connection with the sale of each Co-Promoted Product.

(b) Returned Product. AstraZeneca shall have the sole responsibility and right to accept any returned Co-Promoted Product. Targacept shall not solicit the return of any Co-Promoted Product, but if for any reason Targacept should receive any returned Co-Promoted Product, Targacept shall promptly notify AstraZeneca. Any Co-Promoted Product returned to Targacept shall be shipped by Targacept to AstraZeneca's designated facility, and all reasonable documented shipping costs incurred by Targacept shall be promptly reimbursed by AstraZeneca. Targacept shall advise the customer that made such return that the Co-Promoted Product has been returned to AstraZeneca. Targacept shall complete in all material respects and deliver to AstraZeneca the returned goods form provided by AstraZeneca with respect to any Co-Promoted Product returned by Targacept to AstraZeneca.

(c) Recalled Product. With respect to any actual or proposed recall or market withdrawal of Co-Promoted Product the terms of Section 3.8.3 of the Agreement shall apply, provided that Targacept shall not be deemed to be negligent or in breach of the Agreement or the Co-Promotion Agreement to the extent of any action taken by Targacept in compliance with the training provided by AstraZeneca under the Co-Promotion Agreement, with AstraZeneca's compliance policies that both were provided to Targacept under the Co-Promotion Agreement and training with respect to which has been included in the training program provided to Targacept's Designated Sales Force(s) as described in Section 4(b), or otherwise with direction from AstraZeneca if the activities required by such training, policies or other direction would themselves constitute negligence or breach. At AstraZeneca's request and reasonable expense, Targacept shall assist AstraZeneca in obtaining any Co-Promoted Product, including all samples thereof, that has been recalled or withdrawn from the market.

13. Requests for Medical Information.

(a) Response to Requests. AstraZeneca shall have the exclusive right to respond to all questions or requests for information about a Co-Promoted Product made by any medical professionals or any other Person to Targacept or its sales representatives that either (i) warrant a response beyond the understanding or knowledge of such sales representative or (ii) are beyond the scope of the product labels and inserts or other Promotional Materials for such Co-Promoted Product (a "**PIR**").

(b) Communication of PIRs. Targacept shall, and shall cause its sales representatives to, promptly communicate to the AstraZeneca Information Center or Medical Resources Department all PIRs received by Targacept or such sales representatives.

(c) Communications to Prescribers. In connection with the co-promotion of Co-Promoted Product(s), Targacept shall cause its sales representatives to inform prescribers that they may contact the AstraZeneca Information Center regarding questions or requests for information about the Co-Promoted Product(s) by telephone or by completing a Medical Resource Form and faxing the completed form directly to AstraZeneca Medical Resources at the facsimile number provided on such form. AstraZeneca shall provide Targacept with sufficient quantities of Medical Resource Forms and Targacept shall cause the sales representatives to provide such forms to prescribers.

14. Product Trademarks and Product Copyrights. Targacept shall promote Co-Promoted Product(s) only under the Product Trademarks. AstraZeneca shall grant Targacept a non-exclusive, royalty free license to use the Product Trademarks and Product Copyrights solely for purposes of performing its obligations under the Co-Promotion Agreement, which license shall terminate upon the expiration or earlier termination of the Co-Promotion Agreement for any reason. "**Product Copyrights**" means all copyrightable subject matter included in the product labels and inserts, the Promotional Materials, and the Co-Promoted Product training materials.

15. Insurance. During the term of the Co-Promotion Agreement, at a minimum, and in addition to any insurance obligations under the Agreement, Targacept shall maintain in full force and effect the following types and amounts of insurance:

(a) commercial general liability insurance covering bodily injury, property damage (including loss of use thereof) with limits of $******** each occurrence and $******** general aggregate, including Premises Liability, Personal/Advertising Injury and Contractual Liability coverage for Targacept's indemnification obligations under the Co-Promotion Agreement;

(b) Products Liability insurance with minimum limits of $******** each event and $******** policy aggregate, including contractual liability endorsement;

(c) commercial automobile liability insurance with a $******** combined single limit (bodily injury and property damage) on Targacept owned and non-owned vehicles at any time during the Term;

(d) workers' compensation insurance as required by all Applicable Laws and Employers Liability insurance with limits of not less than $******** each accident, $******** each employee and $******** policy limit;

(e) umbrella or excess liability insurance with limits of $******** each occurrence and $******** general aggregate; and

(f) employment practices liability insurance with limits of $******** per event.

As of the effective date of the Co-Promotion Agreement and from time to time during the Term, Targacept shall upon request from AstraZeneca certify that its general liability, product liability, automobile liability and employers' liability insurance policies are scheduled as "underlying" insurance on its umbrella or excess liability insurance policy(ies).

Each of the policies in Sections 15(a), (b) and (c) shall name AstraZeneca as an additional insured and shall be primary to any liability insurance carried by AstraZeneca, which insurance shall be excess and non-contributory, for claims and losses arising out of Targacept's performance of the Co-Promotion Agreement.

Certificates evidencing at least the above-required insurance coverage shall be submitted by Targacept prior to the commencement of any promotion activities by Targacept and thereafter prior to each renewal or replacement period and shall bear a certification that the coverage specified therein will not be canceled or terminated without at least ******** written notice to AstraZeneca. All such insurances shall be written with one or more companies licensed to do business in the states in which Targacept operates, which companies have a financial rating of not less than ******** in the most current edition of Bests Key Rating Guide.

For the avoidance of doubt, Section 15 shall apply to any CSO retained by Targacept (including pursuant to Section 1(c)).

16. Indemnification.

(a) Indemnification of AstraZeneca. In addition to any other remedy available to AstraZeneca, Targacept shall defend, indemnify and hold harmless AstraZeneca, its Affiliates, all of its and their respective officers, directors, employees and agents and all successors, heirs and assigns of any of the foregoing (collectively, "**AstraZeneca Indemnitees**") from and against any and all Losses incurred by or imposed upon any of them as a result of or arising from Claims arising out of (i) any breach of the Co-Promotion Agreement by Targacept, other than its obligations under Section 5 (for which the sole and exclusive remedy is as set forth in Section 6) or (ii) the material breach of any representation or warranty made by Targacept in the Co-Promotion Agreement, except to the extent such Losses arise as a result of the negligence, fraud, willful misconduct or wrongful act of any AstraZeneca Indemnitee.

(b) Indemnification of Targacept. In addition to any other remedy available to Targacept, AstraZeneca shall defend, indemnify and hold harmless Targacept, its Affiliates, all of its and their respective officers, directors, employees and agents and all successors, heirs and assigns of any of the foregoing (collectively, "**Targacept Indemnitees**") from and against any and all Losses incurred by or imposed upon any of them as a result of or arising from Claims arising out of (i) any breach of the Co-Promotion Agreement by AstraZeneca, (ii) the material breach of any representation or warranty made by AstraZeneca in the Co-Promotion Agreement, (iii) any product liability claim, regardless of the basis of such claim, relating to the treatment of a patient with Co-Promoted Product, (iv) the defective design of a Co-Promoted Product or inherent defects in a Co-Promoted Product, or (v) the use of Promotional Materials without modification and in accordance with the Co-Promotion Agreement, the training provided by AstraZeneca under the Co-Promotion Agreement, Applicable Laws and, to the extent Targacept was given written notice thereof, AstraZeneca's compliance policies for promoting pharmaceutical products, except to the extent such Losses arise as a result of the negligence, fraud, willful misconduct or wrongful act of any Targacept Indemnitee.

(c) With respect to any Claim for which Targacept has an obligation to any AstraZeneca Indemnitee pursuant to Section 16(a) and AstraZeneca has an obligation to any Targacept Indemnitee pursuant to Section 16(b), each Party shall indemnify each of the other Party's Indemnitees for its Losses to the extent of its responsibility, relative to the other Party, for the facts underlying the Claim.

17. Term and Termination.

(a) Term. Unless earlier terminated in accordance with the terms hereof or extended by mutual written agreement of the Parties, the term of the Co-Promotion Agreement (the "**Term**") shall commence on the effective date and continue until AstraZeneca is no longer fielding a sales force for a Co-Promoted Product in the U.S. Territory.

(b) Termination. In addition to any other provision of the Co-Promotion Agreement expressly providing for termination of the Agreement, the Co-Promotion Agreement may be terminated by either Party:

(i) in the event of a material breach of the Co-Promotion Agreement by the other Party, other than a breach of Targacept's obligations under Section 5 (for which the sole and exclusive remedy is as set forth in Section 6), which breach remains uncured ******** after written notice thereof is given to the breaching Party;

(ii) upon ******** written notice to the other Party in the event the FDA recommends or otherwise causes the withdrawal of a Co-Promoted Product from the market at any time after launch for a period in excess of ********;

(iii) immediately upon written notice if the other Party files for protection under bankruptcy or insolvency laws, makes an assignment for the benefit of creditors, appoints or suffers appointment of a receiver or trustee over its property that is not discharged within ******** after such filing, proposes a written agreement of composition or extension of its debts, proposes or is a party to any dissolution or liquidation, files a petition under any bankruptcy or insolvency act or has any such petition filed against it which involuntary petition is not discharged within ******** of the filing thereof; or

(iv) as otherwise set forth in the Agreement.

(c) Suspension. The Co-Promotion Agreement may be suspended by either Party upon ******** written notice to the other Party in the event the FDA recommends or otherwise causes the withdrawal of a Co-Promoted Product from the market at any time after launch for a period in excess of ******** days; provided that the Co-Promotion Agreement shall be reinstated at the request of Targacept if the Co-Promoted Product is subsequently returned to the market prior to the date, if any, that the Co-Promotion Agreement is terminated pursuant to Section 17(b).

(d) Effect of Termination or Expiration. Upon the effective date of termination or expiration of the Co-Promotion Agreement, Targacept immediately shall cease all Detailing and promotion of the Co-Promoted Product(s) and discontinue the use of any Promotional Materials and sample forms.

(e) Return of All Materials. Upon the termination or expiration of the Co-Promotion Agreement, Targacept shall promptly return to AstraZeneca all Co-Promoted Product sample forms, all Promotional Materials, and all training materials that AstraZeneca provided to Targacept pursuant to the Co-Promotion Agreement that are in the possession of, or under the control of, Targacept or its Designated Sales Force(s).

SCHEDULE 7

FORM OF CONFIRMATORY LICENSE AGREEMENT

Date:

Parties:

(1) 'Targacept': Targacept, Inc., a Delaware corporation having its principal place of business at 200 East First Street, Winston-Salem, North Carolina 27101.

(2) 'AstraZeneca': [AstraZeneca Entity], a [_____] having a principal place of business at [_____].

By an Agreement (the 'Main Agreement') dated [_____] and made between Targacept and AstraZeneca Targacept granted for the consideration therein contained to AstraZeneca a license under [UK Patent No _____] [European Patent (UK) No _____] ('the Patent').

Operative provisions:

In pursuance of the Main Agreement and for the consideration referred to in the Main Agreement Targacept hereby confirms the grant to AstraZeneca of the exclusive license from the Effective Date for the term specified in the Main Agreement to manufacture, market, sell and otherwise dispose of Licensed Products (as defined in the Main Agreement) in the Field (as defined in the Main Agreement) for the life of the Patent and subject to the provisions of the Main Agreement.

Subject as provided in the Main Agreement this License shall terminate with respect to a given country without notice in the event of the termination for any reason of the Main Agreement with respect to such country.

IN WITNESS of which this License has been executed as a deed and delivered the day and year first above written.

EXECUTED as a Deed by _____ acting by:

[name of director] and:

[name of director/secretary]

EXECUTED as a Deed by _____ acting by:

[name of director] and:

[name of director/secretary]

SCHEDULE 8

USFRF CONSENT

December 1, 2009

USF Research Foundation, Inc.
Attention: Business Manager
USF Box 30445
Tampa, Florida 33620-3044

Re: **Targacept, Inc. License Agreement**

Ladies and Gentlemen:

Targacept, Inc. ("**Targacept**") and the University of South Florida Research Foundation, Inc. ("**Research Foundation**") are parties to that certain Amended and Restated License Agreement dated March 9, 2004, as amended effective September 21, 2009 (the "**License Agreement**"), whereby Research Foundation granted Targacept an exclusive license under the Patent Rights to research, develop, make, have made, use, market, distribute, lease, sell, import and export Licensed Products and Licensed Processes for any and all indications in the Territory (collectively, the "**Licensed Rights**"). Capitalized terms used herein and not otherwise defined have the respective meanings ascribed to them in the License Agreement.

Targacept desires to enter into a Collaboration and License Agreement with AstraZeneca AB ("**AstraZeneca**") substantially in the form attached hereto as Exhibit A (the "**Collaboration Agreement**"). As would be required by the Collaboration Agreement, Targacept wishes to grant to AstraZeneca a sublicense to the Licensed Rights (the "**Sublicense**"). Targacept hereby requests that Research Foundation approve the Sublicense and otherwise consent to all of the terms of the Collaboration Agreement.

By signing below, Research Foundation hereby: (i) approves, as contemplated by Section 2.5 of the License Agreement, the Sublicense in accordance with the terms of the Collaboration Agreement; (ii) consents to Targacept's subcontract of its rights and obligations to prosecute, maintain, enforce and defend the Patent Rights to AstraZeneca and the right of AstraZeneca to grant sublicenses (through multiple tiers) to the Licensed Rights, in each case subject to the terms and conditions set forth in the Collaboration Agreement and without need for further consent or approval from Research Foundation); and (iii) agrees to hold in confidence the terms of the Collaboration Agreement in accordance with Research Foundation's obligations under Article XV of the License Agreement.

Please sign in the space provided below and return a copy as soon as possible by facsimile, or in PDF format via email, to Pete Zorn, Vice President, Legal Affairs and General Counsel (facsimile number: 336-480-2103; email: pete.zorn@targacept.com), and then mail the originally executed document to the attention of Katy Lusetti at Targacept's address set forth below.

[signature page follows]

Very truly yours,

Targacept, Inc.

By: _____
Name:
Title:

Consented to, approved and agreed:

University of South Florida Research Foundation, Inc.

By: _____
Name:
Title:
Date:

Exhibit A

Collaboration Agreement

SCHEDULE 9

********** CONSENT**

****
****
****
****
Attention: Legal Department

Re: **Targacept, Inc. Master Services Agreement and Work Order No. 1**

Ladies and Gentlemen:

Targacept, Inc. ("**Targacept**") and ********** ("**********") are parties to that certain Master Services Agreement, dated August 13, 2009 (the "**Master Services Agreement**"), and Work Order No. 1, dated August 13, 2009, entered into under the Master Services Agreement ("**Work Order No. 1**" and, together with the Master Services Agreement, the "**Agreement**").

Targacept intends to enter into a Collaboration and License Agreement (the "**Collaboration Agreement**") with AstraZeneca AB (publ) ("**Assignee**"). As would be required by the Collaboration Agreement, Targacept wishes to assign the Agreement and all of Targacept's rights under the Agreement, and delegate all of Targacept's obligations and liabilities under the Agreement, to Assignee (together, the "**Assignment**"), in each case if and as of the date on which the Collaboration Agreement becomes effective by its terms, if any (the "**Assignment Date**"). By signing below, ********** hereby provides its written consent to the Assignment as contemplated by Section 17 of the Master Services Agreement. It is acknowledged and agreed that: (1) the consent of ********** shall be null and void and of no force or effect if Targacept and Assignee have not entered into the Collaboration Agreement on or before December 31, 2009 or if the Collaboration Agreement has not become effective on or before December 31, 2011; and (2) if any Work Order is entered into under the Master Services Agreement by ********** and Assignee after the Assignment Date, the terms and conditions of Work Order No. 1 may not necessarily be incorporated into such Work Order.

Please sign in the space provided below and return a copy as soon as possible by facsimile, or in PDF format via email, to Pete Zorn, Vice President, Legal Affairs and General Counsel (facsimile number: 336-480-2103; email: pete.zorn@targacept.com), and then mail the originally executed document to the attention of Katy Lusetti at Targacept's address set forth below.

[signature page follows]

Very truly yours,

Targacept, Inc.

By: _____
Name:
Title:

Consented to and Agreed:

****

By: _____
Name:
Title:
Date:

SCHEDULE 10

********** MANUFACTURING COSTS**

If a Licensed Product (or placebo) is Manufactured by AstraZeneca or its Affiliate ("**AstraZeneca Manufactured Material**"), AstraZeneca's (or its Affiliate's) ************ costs for Manufacturing such AstraZeneca Manufactured Material shall be include solely the following components:

(a) the following direct Manufacturing costs:

(i) raw materials (including, but not limited to, active pharmaceutical ingredient, process chemicals and excipients, semi-finished materials, primary and secondary packaging components, and consumables used in manufacturing and testing);

(ii) ************ and ************;

(iii) ************; and

(iv) ************ costs that can be directly attributed to such AstraZeneca Manufactured Material, such as ************ and ************ costs, other ************ (e.g., ************), ************, and ************ that can be directly attributed to such AstraZeneca Manufactured Material; and

(b) allocations of ************ and Manufacturing ************ costs, such as ************ and ************ and ************ and ************ on ************ and ************; provided that (i) ************ costs shall be allocated to AstraZeneca Manufactured Material (and other products or materials) using allocation methodologies employed consistently at the site across all brands such as ************ or ************ and ************, (ii) it is the intent of the Parties that the then-existing accounting and allocation methodologies resident at a particular Manufacturing facility be used for determining cost allocation and that cost allocations be fair and equitable and (iii) allocations to AstraZeneca Manufactured Material shall be made based on its ************ relative to the ************ of the ************ used for the ************ over the previous ************ years.

SCHEDULE 11

FRAMEWORK

****

SCHEDULE 12

EXAMPLE CALCULATION OF REDUCTION IN ROYALTIES PURSUANT TO SECTION 5.3.1(c)(i)

The calculation set forth in this Schedule 12 is for illustrative purposes only. Capitalized terms used but not defined in this Schedule 12 shall have the meaning set forth in Article 1 this Agreement.

- ******** Dollars in Net Sales for applicable Licensed Product in ROW Territory (including Country A)
  - ******** Dollars in the ********% royalty tier (********% of total Net Sales in the ROW Territory)
  - ******** Dollars in the ********% royalty tier (********% of total Net Sales in the ROW Territory)
- ******** Dollars in Net Sales for applicable Licensed Product in Country A where the royalty rates are subject to reduction pursuant to Section 5.3.1(c)(i)
  - ******** Dollars in the ********% royalty tier (********% of Net Sales in Country A)
  - ******** Dollars in the ********% royalty tier (********% of Net Sales in Country A)
- Royalties with respect to Net Sales of applicable Licensed Product in ROW Territory excluding Country A:
  - [******** Dollars - ******** Dollars] * ******** = ******** Dollars
  - [******** Dollars - ******** Dollars] * ******** = ******** Dollars
- Royalties with respect to Net Sales of applicable Licensed Product in Country A:
  - ******** Dollars * ******** = ******** Dollars
  - ******** Dollars * ******** = ******** Dollars
- Total royalties payable with respect to Net Sales of applicable Licensed Product in ROW Territory: ******** Dollars

Exhibit 10.21

Description of Annual Cash Incentive Program

Targacept, Inc. (the "Company") maintains an incentive award program (the "Program") under which all of its employees, including its named executive officers, are eligible to receive an annual cash incentive bonus. Under the terms of the Program, each employee is assigned a target bonus percentage of his or her base salary. The target bonus percentages for the Company's named executive officers (and other members of its executive (management) committee) are determined by the Compensation Committee of the Board of Directors. At or about the beginning of each fiscal year, the Compensation Committee establishes performance objectives for the Company for that year and ascribes a percentage weight to each objective. The aggregate weight for all of the performance objectives is at least equal to 100%. The performance objectives may include additional weighting associated with events considered by the Compensation Committee to be particularly challenging that, if achieved, would be expected to provide substantial benefit to the Company and its stockholders. In that event, the aggregate weight for all of the objectives exceeds 100%. The performance objectives typically relate to one or more of the following areas — the discovery, progression or advancement of the Company's product candidates, clinical or nonclinical development, preclinical research, regulatory operations, business development, alliance management, cash management and capital efficiency.

Following the end of the fiscal year, the Compensation Committee determines the achievement level for the Program for that year. In determining the achievement level, the Compensation Committee calculates the weights ascribed to those performance objectives that have been met, the circumstances surrounding any performance objective that has not been met and whether to award all or any portion of the weight ascribed to that objective, and determines whether to make any adjustment based on other Company accomplishments that occurred during the year.

For a group of employees that includes the Company's principal executive officer, principal financial officer and other named executive officers, 100% of the annual cash incentive bonus is determined based on the achievement level for the Program determined by the Compensation Committee as described above. Accordingly, the annual cash incentive bonus for a particular year for each employee in this group is determined by multiplying the amount of his or her base salary received for that year times his or her assigned target bonus percentage times the achievement level for the Program determined by the Compensation Committee. For the Company's remaining employees, 50% of the annual cash incentive bonus is based on the achievement level for the Program determined by the Compensation Committee and the other 50% is based on individual performance.

Exhibit 10.22

Description of Non-Employee Director Compensation Program

Targacept, Inc. (the "Company") maintains a non-employee director compensation program pursuant to which:

- each non-employee director who is first elected or appointed to the Board of Directors after the Company's initial public offering receives a nonqualified option to purchase 25,000 shares of the Company's common stock on the fifth business day after his or her election or appointment (an "Initial Option");

- each non-employee director who is first elected or appointed as chairman of the Board of Directors after the Company's initial public offering receives an additional Initial Option to purchase 10,000 shares of the Company's common stock on the fifth business day after his or her election or appointment;

- each non-employee director receives on an annual basis a nonqualified option to purchase 7,500 shares of the Company's common stock or, in the case of the chairman of the Board of Directors, an option to purchase 12,500 shares of the Company's common stock (an "Annual Option");

- each non-employee director receives an annual cash retainer of $25,000 payable in quarterly installments ($45,000 in the case of the chairman of the Board of Directors); and

- each member of the Audit Committee receives an additional annual cash retainer of $6,000 ($16,000 in the case of the chairman of the committee); each member of the Compensation Committee receives an additional annual cash retainer of $5,000 ($10,000 in the case of the chairman of the committee); and each member of the Governance and Nominating Committee receives an additional annual cash retainer of $5,000 ($10,000 in the case of the chairman of the committee).

Each Initial Option vests and becomes exercisable (i) with respect to one-third of the shares subject to the Initial Option, on the earlier of the first anniversary of the grant date or the last business day before the annual meeting of stockholders that occurs in the next calendar year, provided that the recipient director remains in service on the vesting date, and (ii) with respect to the remaining two-thirds of the shares subject to the Initial Option on a pro rata quarterly basis over the next two years, if the recipient director remains in service as a director during such periods.

Each Annual Option is granted on the fifth business day after the date of the stockholders meeting at which directors are elected, if the recipient director remains in service as a director as of the grant date, and vests and becomes exercisable in full on the earlier of the first anniversary of the grant date or the last business day before the annual meeting of stockholders that occurs in the next calendar year, provided that the recipient director remains in service as a director on the vesting date.

The option price per share for both Initial Options and Annual Options is equal to the fair market value of the common stock as of the date the option is granted, as determined in accordance with the Company's 2006 Stock Incentive Plan (or any successor plan). The option period for both Initial Options and Annual Options is 10 years. Initial Options and Annual Options granted to any director are subject to certain restrictions on exercise if his or her service on the Board of Directors terminates.

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the following Registration Statements:

- Registration Statement (Form S-8 No. 333-133882) pertaining to the Targacept, Inc. 2000 Equity Incentive Plan
- Registration Statement (Form S-8 No. 333-160331) pertaining to the Targacept, Inc. 2006 Stock Incentive Plan
- Registration Statement (Form S-3 No. 333-162379) of Targacept, Inc.

of our reports dated March 11, 2010, with respect to the financial statements of Targacept, Inc. and the effectiveness of internal control over financial reporting of Targacept, Inc., included in this Annual Report (Form 10-K) for the year ended December 31, 2009.

/s/ Ernst & Young LLP

Raleigh, North Carolina
March 11, 2010

Exhibit 31.1

CERTIFICATION

I, J. Donald deBethizy, certify that:

1. I have reviewed this Annual Report on Form 10-K of Targacept, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2010

By: /S/ J. DONALD DEBETHIZY

J. Donald deBethizy
President and Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Alan A. Musso, certify that:

1. I have reviewed this Annual Report on Form 10-K of Targacept, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2010

By: /S/ ALAN A. MUSSO

Alan A. Musso
Vice President, Chief Financial Officer and Treasurer

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of Targacept, Inc. (the "Company") for the period ended December 31, 2009 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, J. Donald deBethizy, President and Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 11, 2010

By: /S/ J. DONALD DEBETHIZY
J. Donald deBethizy
President and Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of Targacept, Inc. (the "Company") for the period ended December 31, 2009 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Alan A. Musso, Vice President, Chief Financial Officer and Treasurer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 11, 2010

By: /S/ ALAN A. MUSSO
Alan A. Musso
Vice President, Chief Financial Officer and Treasurer