



Entelos Inc.

("Entelos" or "the Company")

Interim Results for the six months ended 30 June 2008

Foster City, CA, September 23, 2008 – Entelos, Inc. (LSE: ENTL), the leader in predictive disease simulation for pharmaceutical, health-care and consumer products applications, today announces its interim results for the six months ended 30 June 2008.

Financial Highlights

- Recognized revenue of \$9.6 million for the first half of 2008
- Net loss of \$2.6 million for the first half of 2008
- Cash receipts for the first half of 2008 more than doubled versus the first half of 2007
- Cash and accounts receivable totaled \$8.5 million as at 30 June 2008
- Management believes the Company is on track for double-digit percentage revenue growth for full-year 2008

Operating Highlights

- Entered into an agreement to conduct *in silico* research for UCB Pharma S.A. in rheumatoid arthritis
- Signed an agreement with PDL Biopharma to simulate clinical trials to support PDL's antibody development programs
- Obtained a U.S. patent that expires in 2024 for the mathematical and computer modeling of diabetes
- Entered into an agreement with Unilever to build a new platform and apply Entelos' technology to accelerate Unilever's product development
- Broadened availability of *in silico* testing of "virtual mice", providing Entelos' Type 1 Diabetes Realab platform online to members of the American Diabetes Association
- Entered into a new agreement that extends Entelos' technology applications to risk assessment and reduction in cardiovascular disease in "virtual consumers"
- Selected to participate in a three-year, \$14 million industry-academic consortium funded by Pfizer to identify new targets for diabetes and obesity
- Entered into an agreement with Eli Lilly to conduct *in silico* research in the field of diabetes using the Entelos® Metabolism PhysioLab® platform

Post-Period Announcements

- Obtained a U.S. patent for a gene expression test for liver toxicity screening, which is part of Entelos' DrugMatrix®, the world's largest reference database linking gene expression profiles of over 630 drugs to results from traditional preclinical pharmacology, safety, and toxicity tests
- Entered into an agreement with Eli Lilly for a perpetual license to Entelos' DrugMatrix database and additional customized report services from ToxFx®.

James Karis, Chief Executive Officer of Entelos, said: "We have had solid financial performance over the past six months to the end of June and are pleased to continue attracting pharmaceutical customers as well as expanding our customer base to include consumer products companies. We believe that our outlook remains positive and we look forward to continuing to leverage our predictive technologies to

improve human health.”

Enquiries

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Chairman and Chief Executive's Review

We are pleased to present our financial and operating results for the six months ended 30 June 2008.

Revenues for the six months ended 30 June were \$9.6 million (2007: \$15.7 million) resulting in a net loss of \$2.6 million (2007: net income of \$5.5 million) and a net loss per share (basic) of \$0.04 (2007: net income per share, basic, of \$0.10). During 2007, recognized revenue under US GAAP accounting rules was very uneven due to revenue recognized on contracts upon completion that had been deferred (first half \$15.7 million; second half \$6.1 million). In 2008, revenues will be more ratable (i.e., management expects revenues to be comparable to the level of operating activity on customer contracts). Analysts expect full year 2008 revenues to be higher than 2007 revenues and management believes it is on track to achieve this increase.

There are two other factors that support the financial progress of the Company on a year over year basis. Cash receipts more than doubled year over year (\$7.6 million for the first six months of 2008 versus \$3.7 million for the first six months of 2007); and cost of revenue increased 91% (\$6.0 million for the first six months of 2008 versus \$3.2 million for the first six months of 2007). Cost of revenue represents the labor cost of employees working on customer contracts and the related travel and overhead costs.

Investment in R&D for the six months ended 30 June was \$1.5 million (2007: \$4.6 million) due to reduced requirements for technology development and the re-deployment of resources to customer contracts. Sales and marketing expenses increased to \$1.5 million (2007: \$0.9 million) as the Company expanded the number of business development resources. Management plans to continue this increased investment in the second half of 2008. General and administrative expenses increased to \$2.8 million (2007: \$1.7 million) primarily due to non-cash intangible asset amortization and stock compensation expense as well as some additional spending on patent costs.

As of 30 June 2008, the Company had cash and accounts receivable of \$8.5 million (2007: \$5.7 million). Management believes the Company is on track to achieve its 2008 plans and is in compliance with all debt covenants for the first two quarters of the year.

Collaborative Partners and Predictive Platforms

Entelos partners with global pharmaceutical, biotechnology, and consumer products companies to support their product development activities. We apply our core predictive technologies to key applications in the R&D process, including validating novel drug targets, selecting compounds, translating results from animal models to predict human responses, evaluating new product opportunities, and better positioning existing products in competitive markets. During the first half of 2008, the Company made progress across multiple areas:

- New Customer Contracts, Pharmaceutical or Biotechnology Companies: Entelos announced agreements to conduct *in silico* research with UCB Pharma, PDL Biopharma, and Eli Lilly across multiple disease areas.
- New Contracts and New Technology Applications, Outside the Pharmaceutical Industry: Entelos entered into an agreement to collaborate with Unilever to develop a new PhysioLab platform that will complement Unilever's internal capabilities and create a powerful integrated discovery platform to accelerate Unilever's product development. This is the second platform development contract with this customer following a collaboration in skin sensitization designed to reduce animal testing. In addition, Entelos entered into a new agreement with another customer that extends Entelos' technology applications to risk assessment and reduction in cardiovascular disease in "virtual consumers", representations of unique genetic, biologic, and lifestyle profiles.
- New Industry-Academia Consortium: Entelos was the only company selected to join a unique three-year, \$14 million industry-academic consortium funded by Pfizer to identify new targets for diabetes and obesity. The consortium, called the Insulin Resistance Pathways Project (IRP Project), is comprised of top researchers from the University of California, Santa Barbara (UCSB), the California Institute of Technology (Caltech), the Massachusetts Institute of Technology (MIT), the University of Massachusetts (UMass), Entelos, and several research groups from within Pfizer. The goal of the IRP Project is identify drug targets within cells which will ultimately lead to a compelling new class of diabetes drugs—drugs that will relieve insulin resistance, a major factor in diabetes and obesity.
- Intellectual Property: Entelos obtained U.S. patent #7,353,152 that expires in 2024 for the diabetes model. This patent relates to the mathematical and computer modeling of multiple biological processes underlying the Entelos® Metabolism PhysioLab® platform, which can be applied to obesity as well as diabetes research. The Company now owns 35 patents and over 130 pending applications worldwide on its PhysioLab models, software platform, and biological insights arising from its use.
- Technology Access: The American Diabetes Association broadened the availability of *in silico* testing of "virtual mice" by providing its members Entelos' Type 1 Diabetes Realab platform online. This platform enables researchers to conduct powerful "what if" experiments prior to initiating expensive and time-consuming laboratory studies in mice.

In addition, Entelos has made significant progress with other ongoing customer contracts across multiple disease areas and continues to attract customers from both the pharmaceutical and consumer products sectors.

Post-Period announcements

- Iconix Biosciences, acquired by Entelos about one year ago, obtained a U.S. patent for a gene expression test for liver toxicity screening, which is now part of Entelos' DrugMatrix®, the world's largest reference database linking gene expression profiles of over 630 drugs to results from traditional preclinical pharmacology, safety, and toxicity tests. Entelos customers using DrugMatrix can thus predict safety and toxicity liabilities of novel molecules using much shorter, faster, and more cost-effective gene expression studies as compared to traditional methods.
- Finally, Entelos entered into an agreement with Eli Lilly for a perpetual license to Entelos' DrugMatrix database and additional customized report services from ToxFx®. Thus, Entelos is offering both cutting-edge safety prediction technology and *in silico* research to help accelerate Lilly's drug research programs.

Strategy & Outlook

Entelos has grown to become the leader in providing predictive disease simulation technology and services and toxicogenomics solutions to pharmaceutical, health-care and consumer products companies. Management believes that the Company continues to maintain its leadership position for the following key reasons:

- Unique predictive technologies relative to competitive solutions
- World-class customer base and partnerships and long-term customer relationships

- A customer base that is highly attracted to solutions that reduce animal testing, increase the probability of clinical trial success, and result in savings in cost and time to market
- Strong support from the FDA for modeling and simulation technology adoption and integration to accelerate drug approval
- A predictive “virtual human” technology platform that has a wide and growing array of applications, from pharmaceutical research and development to consumer products, food and nutrition and personalized health care

“While we are pleased with these accomplishments, we are disappointed that our share price does not reflect the uniqueness of our science, the growing success of our marketing, and the sustained improvement in our financial performance,” stated Jon Saxe, Entelos’ Chairman of the Board. “We hope that the continuing successful development of the Company is soon reflected in the share price.”

We are thus determined to expand our capabilities, increase adoption within our customer base, and build shareholder value by:

- Continuing to demonstrate our technology’s impact and value for lowering the risk, time, and cost of drug discovery and development
- Assessing safety at an earlier stage of the R&D process
- Using our predictive technologies, alliances, and partnerships to help our customers discover and develop new therapeutics in a more cost-effective manner
- Salvaging therapeutic programs and initiatives through reprofiling and repositioning; that is, finding new uses and indications for existing drug programs

Our strategy thus focuses on the following key points:

- Continue to build more models and acquire complementary predictive technologies for efficacy and safety testing to generate revenue from services and technology licensing
- Continue to productize the core technology by creating specific, targeted applications to address key R&D processes and creating new products and offerings that allow greater customer access to our suite of predictive technologies
- Continue to expand the availability of technology through licenses and subscriptions
- Significantly expand business development and sales efforts
 - Expand customer base geographically by further developing European presence and entering Asian markets
 - Expand customer base by industry through sales strategy targeting biotech, consumer products and healthcare companies
- Enter new markets, particularly in personalized medicine, where an increasingly amount of new genetic, diagnostic, and imaging data need to be combined with medical histories and other critical tests to help provide an integrative, holistic view of individual patients to dramatically improve patient choice, care, and outcomes.

We continue to be excited about Entelos’ corporate growth prospects and look forward to more success in the future.

Jon Saxe
Chairman of the Board
 23 September 2008

James Karis
President and Chief Executive Officer

Entelos, Inc.

Unaudited Interim Condensed Balance Sheet

	<u>31 December</u>	<u>30 June</u>
	<u>2007</u>	<u>2008</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 5,260,079	\$ 4,144,579
Accounts receivable	4,693,409	4,379,766
Prepaid expenses and other current assets	464,867	364,358
Total current assets	<u>10,418,355</u>	<u>8,888,703</u>
Property and equipment, net	1,826,668	1,537,050
Intangible assets, net	926,284	572,712
Goodwill	8,368,847	8,368,847
Notes receivable from related parties	723,795	737,086
Other assets	450,276	435,053
Total assets	<u>\$ 22,714,225</u>	<u>\$ 20,539,451</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 900,911	\$ 201,522
Accrued liabilities	1,806,289	1,543,512
Accrued compensation	2,680,665	2,883,918
Deferred revenue	5,706,813	3,369,480
Notes payable, current	-	1,638,579
Total current liabilities	<u>11,094,678</u>	<u>9,637,011</u>
Long-term debt	4,324,645	5,309,061
Other	37,200	239,339
Total liabilities	<u>15,456,523</u>	<u>15,185,411</u>
Stockholders' equity		
Common stock	69,093	69,093
Additional paid-in capital	81,354,047	82,007,831
Deferred stock-based compensation	(148,864)	(93,447)
Accumulated deficit	(74,016,574)	(76,629,437)
Total stockholders' equity	<u>7,257,702</u>	<u>5,354,040</u>
Total liabilities and stockholders' equity	<u>\$ 22,714,225</u>	<u>\$ 20,539,451</u>

The accompanying notes are an integral part of these unaudited interim condensed financial statements

Entelos, Inc.

Unaudited Interim Condensed Statement of Operations

	Six Months Ended 30 June	
	2007	2008
Revenues	\$ 15,719,551	\$ 9,582,939
Operating costs and expenses:		
Cost of revenue	3,153,468	6,017,616
General and administrative	1,701,847	2,822,920
Research and development	4,612,417	1,523,600
Sales and marketing	914,925	1,527,945
Total operating costs and expenses	<u>10,382,657</u>	<u>11,892,081</u>
Income (loss) from operations	5,336,894	(2,309,142)
Interest income	133,560	63,295
Interest expense	(5,380)	(411,384)
Other income (expense), net	<u>(1,286)</u>	<u>44,368</u>
Net income (loss)	<u>5,463,788</u>	<u>(2,612,863)</u>
Net income (loss) per share - basic and diluted		
Net income (loss) per share — basic	<u>\$ 0.10</u>	<u>\$ (0.04)</u>
Net income (loss) per share — diluted	<u>\$ 0.10</u>	<u>\$ (0.04)</u>
Weighted average common shares outstanding used in calculating net income (loss) per common share:		
Basic	<u>53,353,952</u>	<u>69,109,387</u>
Diluted	<u>56,625,142</u>	<u>69,109,387</u>

The accompanying notes are an integral part of these unaudited interim condensed financial statements

Entelos, Inc.

Unaudited Interim Condensed Statements of Cash Flows

	Six Months Ended 30 June	
	2007	2008
Cash flows from operating activities:		
Net income (loss)	\$ 5,463,788	\$ (2,612,863)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation and amortization	513,642	833,418
Stock-based compensation	455,638	706,654
Amortization of discount on notes payable	-	159,101
Loss on disposal of assets	-	26,707
Changes in assets and liabilities:		
Accounts receivable	(1,236,872)	313,643
Prepaid expenses, notes receivable and other assets	(269,746)	102,440
Accounts payable	(191,169)	(699,389)
Accrued liabilities	386,800	177,565
Accrued compensation	514,224	405,392
Deferred revenue	(10,840,821)	(2,337,333)
Net cash used in operating activities	<u>(5,204,516)</u>	<u>(2,924,665)</u>
Cash flows from investing activities:		
Purchase of short-term investments	(1,489,026)	-
Sales of short-term investments	4,756,377	-
Purchases of property and equipment	(223,604)	(179,747)
Net cash provided by (used in) investing activities	<u>3,043,747</u>	<u>(179,747)</u>
Cash flows from financing activities:		
Proceeds from issuance of common stock	73,692	-
Proceeds from issuance of notes payable	-	2,000,000
Repayment of notes payable	(105,106)	(11,088)
Net cash provided by (used in) financing activities	<u>(31,414)</u>	<u>1,988,912</u>
Net decrease in cash and cash equivalents	(2,192,183)	(1,115,500)
Cash and cash equivalents at beginning of period	4,702,426	5,260,079
Cash and cash equivalents at end of period	<u>\$ 2,510,243</u>	<u>\$ 4,144,579</u>
Supplemental disclosures of cash flow information:		
Interest paid	<u>\$ 4,273</u>	<u>\$ 2,672</u>
Supplemental disclosure of noncash financing activities:		
Capital leases	<u>\$ -</u>	<u>\$ 239,809</u>
Reclassification from liability of early exercised shares	<u>\$ 9,491</u>	<u>\$ 2,547</u>

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ENTELOS, INC.
NOTES TO UNAUDITED INTERIM CONDENSED FINANCIAL STATEMENTS

NOTE 1 - The Company and Summary of Significant Accounting Policies

The Company

Entelos, Inc (the "Company") was incorporated in the state of California on 31 July 1996. On 4 April 2006, the Company reincorporated from the State of California into the State of Delaware. On 12 April 2006, the Company completed an initial public offering on the Alternative Investment Market of the London Stock Exchange ("AIM") for the sale of 13,810,173 common shares which raised \$16.6 million of net proceeds.

Entelos is a US-based life sciences company that develops and applies next generation predictive technologies to reduce the risk, time, and cost of drug discovery and development. The Company's portfolio of proprietary computer models and toxicology reference systems—known as PhysioLab® and DrugMatrix® systems, respectively—have helped its pharmaceutical customers select novel compounds, assess drug safety, simulate clinical trials and patient populations, evaluate in-licensing candidates, and better position existing products in competitive markets. The Company currently provides research services, technology, and scientific expertise in toxicology screening, asthma, obesity, diabetes, cardiovascular disease, rheumatoid arthritis, hematopoiesis (anemia), cholesterol metabolism, and skin sensitization. The Company's PhysioLab® systems provide a platform for creating "virtual patients" and virtual populations that can also be extended to other applications in medical education, patient support, healthcare delivery, nutritionals, and consumer products.

Going concern uncertainty

The Company has incurred significant operating losses since inception and will continue to be in a net loss position until sufficient revenues can be generated to offset expenses. In 2007, the Company obtained \$6.5 million of debt financings that contains covenants pertaining to liquid assets, net working capital and quarterly operating income. If the Company does not meet the covenants it could result in the debt holder calling a portion or all the debt. Management intends to continue to finance operations of the Company through a combination of future cash flows from operations, cost reduction measures, licensing of rights to existing compounds and if necessary, future debt/equity financings. There can be no assurance that the Company will be successful in obtaining additional financing on favorable terms, or at all. If additional funds are raised by issuing equity securities, substantial dilution to existing shareholders may result. These matters raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Risks and uncertainties

The Company is subject to all of the risks inherent in a company which operates in the intensely competitive service industry, providing a service which is relatively new and constantly evolving. These risks include, but are not limited to: the Company's ability to convince prospective strategic partners and customers that its technology is an attractive component of pharmaceutical research and development; the willingness and ability of customers to adopt new technologies; its customers' perception that the Company's technologies can help accelerate efforts and reduce costs in drug development; and the Company's ability to sell and support sufficient numbers of customer projects.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and such differences could affect the results of operations reported in future periods.

Revenue Recognition

The Company is using its patented PhysioLab® technology to derive revenue from research and development collaboration contracts. Collaboration agreements involve development of and research using dynamic computer models of human diseases, and typically require payments from customers for

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technology access fees, research and development funding, milestone payments (which can be either success-based or delivery-based), or a combination of these elements.

When software is not incidental to the arrangement and the services in the arrangement do not involve significant production, modification, or customization of the software, the Company recognizes revenue in accordance with Statement of Position No. 97-2, "Software Revenue Recognition" ("SOP 97-2"), as amended. Revenue from multiple-element arrangements is allocated to each individual element based on vendor specific objective evidence. Amounts billed but not yet recognized as revenue, and other payments received prior to recognition of revenue, are recorded as deferred revenue.

When the arrangement requires significant production, modification or customization of software, the entire arrangement is accounted in accordance with SOP 81-1 "Accounting for Performance of Construction-Type and Certain Production-Type Contracts", as required by SOP 97-2. For arrangements for which the costs to complete a project can not be reasonably and reliably estimated, the completed contract method of accounting is used. Under the completed contract method, revenue is recognized only when a contract is completed or substantially complete.

For arrangements consisting solely of services, we recognize revenue in accordance with Securities and Exchange Commission Staff Accounting Bulletin No. 104 ("SAB 104"). Arrangements with multiple elements are accounted for in accordance with EITF 00-21, "Revenue Arrangements with Multiple Deliverables." Revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed and determinable and collectibility is reasonably assured.

Certain agreements may define specific milestones and the payments associated with each milestone. Such payments are recognized as revenue upon achievement of the milestone events, after which there are no future performance obligations to this payment. Any payments received in advance of the completion of the milestone are recorded as deferred revenue.

Reimbursements received from customers for out-of-pocket expenses are classified as revenue, with the associated costs included in cost of revenue.

Segment Reporting

We organize ourselves as one segment reporting to the chief operating decision-maker. We have customers outside of the United States, but a significant amount of the work is performed in the United States. All long-lived assets are maintained in the United States.

Fair Value Measurements

Effective 1 January 2008, the Company adopted SFAS No. 157, "Fair Value Measurements", ("SFAS 157"), which defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. SFAS 157 establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 – Directly or indirectly observable market based inputs used in models or other valuation methodologies.

Level 3 – Unobservable inputs that are not corroborated by market data which require significant management judgment.

The Company's adoption of SFAS 157 did not have a material impact on its financial statements. The Company has segregated all financial assets and liabilities at fair value on a recurring basis (at least annually) into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date in the table below. FASB Staff Position (FSP FAS 157-2 – Effective Date of FASB Statement No. 157), or FSP FAS 157-2, delayed the effective date for all nonfinancial assets and liabilities until 1 January 2009, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis. As of 30 June 2008, the embedded derivative

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related to the convertible notes, as discussed below, is measured at fair value using level III inputs.

Effective 1 January 2008, the Company adopted SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment of FASB Statement No. 115", ("SFAS 159"), which provides entities the option to measure many financial instruments and certain other items at fair value. Entities that choose the fair value option will recognize unrealized gains and losses on items for which the fair value option was elected in earnings at each subsequent reporting date. The Company has currently chosen not to elect the fair value option for any items that are not already required to be measured at fair value in accordance with GAAP.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

	Fair Value Measurements at 30 June 2008			
Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Carrying Value at 30 June 2008	
Derivatives	-	-	(684,577)	(684,577)

The following table provides a reconciliation of the beginning and ending balances for assets and liabilities measured at fair value using significant unobservable inputs (Level 3):

Beginning balance at 31 December 2007	\$ (363,298)
Change in fair value, included in interest expense	(34,937)
Increase in level 3	(286,342)
Ending Balance at 30 June 2008	\$ (684,577)

Recent pronouncements

In November 2007, the Emerging Issues Task Force, or EITF, issued EITF Issue 07-01 "Accounting for Collaborative Arrangements", ("EITF 07-01"). EITF 07-01 requires collaborators to present the results of activities for which they act as the principal on a gross basis and report any payments received from (made to) other collaborators based on other applicable GAAP or, in the absence of other applicable GAAP, based on analogy to authoritative accounting literature or a reasonable, rational, and consistently applied accounting policy election. Further, EITF 07-01 clarified that the determination of whether transactions within a collaborative arrangement are part of a vendor-customer (or analogous) relationship subject to EITF Issue 01-9, "Accounting for Consideration Given by a Vendor to a Customer". EITF 07-01 is effective for fiscal years beginning after 15 December 2008. The Company has not yet completed its evaluation of EITF 07-01, but does not currently believe that it will have a material impact on the results of operations, financial position or cash flows of the Company.

On 4 December 2007, the FASB issued SFAS No. 141 (Revised 2007), "Business Combinations", ("SFAS No. 141R"). Under SFAS No. 141R, an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition date fair value with limited exceptions. SFAS No. 141R will change the accounting treatment for certain specific items, including:

- acquisition costs will be generally expensed as incurred;
- noncontrolling interests will be valued at fair value at the acquisition date;
- acquired contingent liabilities will be recorded at fair value at the acquisition date and subsequently measured at either the higher of such amount or the amount determined under existing guidance for non-acquired contingencies;
- in-process research and development will be recorded at fair value as an indefinite-lived intangible asset at the acquisition date until the completion or abandonment of the associated research and development efforts;
- restructuring costs associated with a business combination will be generally expensed subsequent to the acquisition date; and
- changes in deferred tax asset valuation allowances and income tax uncertainties after the acquisition date

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generally will affect income tax expense.

SFAS No. 141R also includes a substantial number of new disclosure requirements. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 15 December 15 2008. Earlier adoption is prohibited. The Company is currently assessing the impact of this statement but believes it will not have a material impact on its financial position, results of operations, or cash flows upon adoption.

In April 2008, the FASB issued FASB Staff Position, FSP SFAS No. 142-3, "Determination of the Useful Life of Intangible Assets" ("FSP SFAS No. 142-3"), which amends the factors that must be considered in developing renewal or extension assumptions used to determine the useful life over which to amortize the cost of a recognized intangible asset under SFAS No. 142, "Goodwill and Other Intangible Assets." FSP SFAS No. 142-3 requires an entity to consider its own assumptions about renewal or extension of the term of the arrangement, consistent with its expected use of the asset, and is an attempt to improve consistency between the useful life of a recognized intangible asset under SFAS No. 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141, "Business Combinations." FSP FAS No. 142-3 is effective for fiscal years beginning after 15 December 2008, and the guidance for determining the useful life of a recognized intangible asset must be applied prospectively to intangible assets acquired after the effective date. The Company is currently assessing the impact of this statement, but believes it will not have a material impact on its financial position, results of operations, or cash flows upon adoption.

In May 2008, the FASB issued Financial Accounting Standard No. 162, "The Hierarchy of Generally Accepted Accounting Principles" ("SFAS No. 162"). The statement is intended to improve financial reporting by identifying a consistent hierarchy for selecting accounting principles to be used in preparing financial statements that are prepared in conformance with GAAP. Unlike SAS No. 69, "The Meaning of Present in Conformity With GAAP," SFAS No. 162 is directed to the entity rather than the auditor. The statement is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, "The Meaning of Present Fairly in Conformity with GAAP." The Company is currently assessing the impact of this statement, but believes it will not have a material impact on its financial position, results of operations, or cash flows upon adoption.

In May 2008, the FASB issued FSP APB 14-1, "Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)" ("FSP APB 14-1"). FSP APB 14-1 requires the liability and equity components of convertible debt instruments to be separately accounted for in a manner that reflects the non-convertible debt borrowing rate for interest expense recognition. In addition, direct issuance costs associated with the convertible debt instruments are required to be allocated to the liability and equity components in proportion to the allocation of proceeds and accounted for as debt issuance costs and equity issuance costs, respectively. FSP APB 14-1 will be effective for fiscal years beginning after 15 December 2008, and interim periods within those fiscal years. FSP APB 14-1 must be applied retrospectively and early adoption is prohibited. The Company is currently evaluating the expected impact of the provisions of FSP APB 14-1, but believes it will not have a material impact on its financial position, results of operations, or cash flows upon adoption.

In June 2008, the FASB issued FASB Staff Position, or FSP, EITF No. 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities." Under the FSP, unvested share-based payment awards that contain rights to receive nonforfeitable dividends (whether paid or unpaid) are participating securities, and should be included in the two-class method of computing EPS. The FSP is effective for fiscal years beginning after 15 December 2008, and interim periods within those years. The Company believes the statement will not have a material impact on its financial position, results of operations, or cash flows upon adoption.

Reclassifications

Certain reclassifications have been made to year end balances to conform to current year presentation.

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NOTE 2 – NET INCOME (LOSS) PER SHARE

Basic net income (loss) per share attributed to common shares is computed by dividing the net income (loss) attributable to common shares for the year by the weighted average number of common shares outstanding during the year as reduced by the weighted average unvested common shares subject to repurchase by the Company. Diluted net income (loss) per share is computed using the weighted average number of common and potential common shares outstanding. Potential common shares include long-term incentive awards, convertible debentures, common stock subject to repurchase rights, and an incremental number of shares of common stock issuable upon the exercise of stock options and warrants. Potential common shares are excluded from the computation if their effect is anti-dilutive.

	Six Months Ended 30 June	
	2007	2008
Weighted average common shares outstanding	53,353,952	69,109,387
Dilutive effect of stock options	1,283,688	-
Dilutive effect of long-term incentive awards	1,987,502	-
Denominator for diluted net income (loss) per share	56,625,142	69,109,387

The potential shares, which are excluded from the determination of diluted net income (loss) per share as their effect is anti-dilutive, are as follows:

	Six Months Ended 30 June	
	2007	2008
Warrants to purchase common stock	269,803	1,213,379
Options to purchase common stock	273,000	3,328,173
Common stock reserved for long-term incentive plan	-	6,956,305
Convertible debentures	-	10,964,037
Shares subject to repurchase	-	7,597
	542,803	22,469,491

NOTE 3 – RELATED PARTY TRANSACTIONS

At 30 June 2008, the Company held full recourse notes receivable from three employees with total balances of \$737,086. The interest rates on these notes range from 1.62 per cent to 3.11 per cent per annum. The notes mature in 2011.

The Company has entered into various collaboration agreements with Pfizer, Inc. (whose subsidiary, Pfizer Overseas Pharmaceuticals is a shareholder of the Company with effect from February 2005) to provide consulting and research related services on drug development. Under the collaboration agreements, the Company has recognized revenues amounting to \$806,491 in the first six months of 2008 and did not recognize revenue for the first six months in 2007.

NOTE 4 – ACQUISITION

Iconix BioSciences, Inc.

In August 2007 the Company acquired Iconix BioSciences, Inc., a privately held predictive toxicology company located in Mountain View, CA. The initial consideration of \$6,459,702 was satisfied by the issuance of 9,278,771 shares of the Company's common stock valued at \$6,075,265 plus acquisition related cost of \$384,436. The acquisition was accounted for using the purchase method and, accordingly, the purchase price has been allocated to the assets acquired and liabilities assumed based on estimated fair values at the date of acquisition. The allocation of the purchase price was as follows:

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Current assets.....	\$ 586,450
Fixed assets	446,668
Other assets	13,333
Technology.....	223,000
Customer Relationships.....	939,000
Goodwill	8,368,847
Total assets acquired.....	<u>10,577,298</u>
Current liabilities.....	(2,274,925)
Deferred revenue.....	(305,471)
Notes payable.....	(1,500,000)
Other liabilities.....	(37,200)
Total liabilities assumed.....	<u>(4,117,596)</u>
Net assets acquired.....	<u>\$ 6,459,702</u>

Valuing certain components of the acquisition, including certain assets and accrued expenses requires the Company to make estimates that may be adjusted in the future; consequently the purchase price allocation is considered preliminary. Final determination of these estimates could result in adjustment to the preliminary purchase price allocation, with an offsetting adjustment to goodwill.

Upon the closing of the above transaction, the Company also became contingently liable for up to an additional \$25 million worth of common stock in the event that certain revenue goals are met through 31 August 2008. The contingent consideration is based on the designated stock price, as defined in the purchase agreement, and will be recorded as purchase price and allocated to goodwill. In accordance with the purchase agreement, 7,935,328 shares of common stock are held in escrow related to the contingent consideration. The parties to the agreement have up to 35 business days after 31 August 2008 to finalize the contingency.

The goodwill, technology, and customer relationships are recorded on the balance sheet as intangibles. None of the goodwill is deductible for tax purposes. The goodwill represents benefits of the acquisition that are additional to the fair value of the other net assets acquired. The primary reasons for the acquisition and the principal factors that contributed to the purchase price that resulted in the recognition of goodwill were as follows:

- Iconix’s predictive toxicology capability combined with Entelos’ predictive *in silico* disease models will address the pharmaceutical industry’s two biggest issues around failures: safety and efficacy.
- Iconix’s DrugMatrix system has been installed at the U.S. Food and Drug Administrative (FDA) for use by the Center for Drug Evaluation and Research (CDER) to evaluate voluntarily genomic data submissions. In addition, Iconix is a member of the Predictive Safety Testing Consortium, which is developing data and processes to support the regulatory use of new safety biomarkers.
- This acquisition of Iconix, as well as the Company’s collaboration with the FDA to develop a predictive model of drug-induced human liver injury, expands the combined companies’ reach into safety assessment.
- Iconix’s technology will also add significant new capabilities for translational medicine and for finding new uses for existing drugs and drug combinations.

The acquired goodwill and intangibles are recorded on the balance sheet as intangibles and other assets. The intangible assets are being amortized over their useful lives:

Technology.....	5 years
Customer Relationships (Platform Alliance Customers).....	1.4 years
Customer Relationships (Service Customers).....	3 years

Goodwill was not subject to amortization. Amortization expense relating to the intangibles totaled \$0, and \$353,567, for the periods ending 30 June 2007 and 2008, respectively.

NOTE 5 – STOCK OPTION AND AWARD PLANS

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1997 Stock Option Plan

On 12 June 1997, the Company adopted the 1997 Stock Plan (the "1997 Plan") under which 7,153,552 shares of the Company's common stock were reserved for issuance to employees, directors and consultants. Options granted under the 1997 Plan may be incentive stock options or nonqualified stock options. Incentive stock options ("ISO") may only be granted to employees of the Company. The nonqualified stock options ("NSO") may be granted to Company employees, directors and consultants. Options to purchase shares of the Company's common stock are granted at a price equal to the fair value of the stock at the date of grant, as determined by the Board of Directors. The exercise price of an ISO granted to an employee who owns more than 10 per cent of the voting power of all classes of stock of the Company shall not be less than 110 per cent of the fair value per share on the date of grant. Generally options terminate ten years after the date of the grant. ISO's granted to employees who own more than ten per cent of the total stock of the Company terminate five years from the date of the grant. The options generally vest over a four year period, 25 per cent after one year and the balance monthly thereafter. The 1997 Plan has been replaced with the 2006 Equity Plan (the "2006 Plan"), cancellations of non vested options from this plan are not added back for future grants.

The 2006 Plan

On 28 March 2006, the Company adopted the 2006 Plan under which 2,000,000 shares of the Company's common stock have been reserved for issuance to employees, directors and consultants. Options granted under the 2006 Plan may be ISO's, restricted stock awards, and NSO's to employees, directors and consultants. ISO's may be granted to current employees only. NSO's and restricted stock awards may be granted to employees, directors and consultants. ISO's may be granted with an exercise price of no less than 100% of the market value of the underlying common shares on the date of grant. NSO's and restricted stock awards may be granted with an exercise price or purchase price of no less than 85 per cent of the market value of the underlying common shares on the date of grant. No option shall be exercisable after its expiration date or have an expiration date that is more than ten years (five years in the case of a 10 per cent shareholder) after the date of grant.

The following table summarizes option activity under both stock option plans:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Outstanding at 1 January 2008.....	3,216,432	\$ 0.50	
Granted.....	276,000	0.49	
Exercised.....	-	-	
Expired or forfeited.....	<u>(164,259)</u>	0.85	
Outstanding at 30 June 2008.....	3,328,173	\$ 0.49	6.84
Options exercisable at 30 June 2008.....	2,411,951	\$ 0.37	5.78

Long-Term Incentive Stock Plan

On 25 September 2007 and 5 April 2006, the Remuneration Committee of the Board of Directors granted performance stock awards pursuant to the Long Term Incentive Plan (the "LTIP"). Under the LTIP common stock is awarded to Executive Directors and senior managers conditional upon the achievement of specific measurable performance criteria determined by the Remuneration Committee. In particular, the Company's total shareholder return ("TSR") is measured against the TSR of companies comprised in an appropriate comparator group set by the Remuneration Committee.

The number of shares granted, net of cancellations, under the 2006 and 2007 LTIP awards was 6,956,305 (1,987,502 in 2006 and 4,968,8031 in 2007). During the periods ended 30 June 2007 and 2008, compensation expense and additional paid-in capital of approximately \$348,454 and \$614,980 was recorded in relation to the stock-based 2006 and 2007 LTIP awards. Compensation expense during the year ended 31 December 2007 was based on the fair value of the awards at date of grant. As of 30 June 2008 there was approximately \$1,868,112 of total unrecognized compensation expense related to the LTIP. Shares awarded under the 2006 and 2007 LTIP awards vest at the end of the three year period subject to the Company achieving specified performance targets measured as of the end of the three year period. The awards are recognized in expense on a straight-line basis over the life of the award.

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In February 2008, the LTIP was amended to allow for cash awards. Under the 2008 award, Executive Directors and senior managers may earn up to two (2) times their salary conditional upon the same criteria as mentioned above. As of 30 June 2008, \$202,139 has been expensed under the 2008 LTIP award and was included in long-term other liabilities.

Stock Based Compensation

Through 31 December 2005, the Company accounted for stock-based employee compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," ("APB No. 25") and complied with the disclosure provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"). Under APB No. 25, compensation cost is recognized based on the difference, if any, on the date of grant between the fair value of the Company's stock and the exercise price. SFAS No. 123 defines a "fair value" based method of accounting for an employee stock option or similar equity investment.

Effective 1 January 2006, the Company adopted SFAS No. 123 (revised 2004), "Share-Based Payments" ("SFAS No. 123R") using the prospective-transition method. Under this transition method, stock compensation cost recognized beginning 1 January 2006 includes compensation cost for all share-based payments granted on or subsequent to 1 January 2006 based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R and compensation expense on the remaining unvested awards under the intrinsic-value method of APB No. 25 for options granted prior to the SFAS 123R effective date.

The Company uses the Black-Scholes-Merton option-pricing model with the following assumptions to estimate the share-based compensation expense for the periods ending 30 June 2007 and 2008, respectively: weighted-average risk-free interest rate of 4.73 and 3.03 per cent based on the U.S. Treasury yield for a period consistent with the expected term of the option in effect at the time of grant; no expected dividend payments; expected life of 4.61 and 4.81 years; weighted-average volatility factor of 56 and 56 per cent based on peer group analysis. Total compensation expense under SFAS 123R for the six-month periods ending 30 June 2007 and 2008 was \$390,140 and \$651,237, respectively; \$41,686 and \$36,256 was related to the 1997 and 2006 stock option plans and \$348,454 and \$614,980 was recorded in relation to the LTIP.

The Company has not been public for a sufficient period of time to use its own volatility. Therefore, the Company used the average volatility of similar entities. Four out of the five companies used as guideline companies are U.S. publicly traded companies that have disclosed their volatility assumptions for the periods ending 30 June 2008 or 31 March 2008 whichever is available. The Company used historical exercise data from the Company's inception for the basis of estimating the expected term.

During 2005 and 2004 options were granted to employees at exercise prices that were less than the fair market value of the common shares on the date of grant which resulted in deferred compensation of \$586,000.

Amortization of deferred stock compensation is recognized on a straight-line basis over the vesting period, reduced by cancellations of unvested options. Amortization of deferred stock compensation for the period ending 30 June 2007 and 2008 was \$65,498, and \$55,417, respectively.

NOTE 6 – NOTES PAYABLE

Senior Secured Note and Convertible Debentures

On 21 December 2007, the Company entered into a debt financing agreement with Imperium Master Fund, LTD ("Imperium") in which Imperium provided \$6,500,000 in total cash loan proceeds. The Company used \$1,500,000 of the proceeds to repay certain debt of Iconix Biosciences, Inc. assumed in the acquisition (See Note 4) and the \$5,000,000 is being used for long-term working capital needs.

The financing provides the Company with \$1,500,000 under a secured bridge note and \$5,000,000 under secured convertible debentures. At the closing of the financing, the Company received a total of \$4,423,888, representing the \$4,500,000 total proceeds from the bridge note and initial debenture less certain expenses of Imperium agreed to be paid by the Company in connection with the transaction. The expenses were recorded as a deferred charge, are included in Other assets on the balance sheets and will be amortized as interest expense on a straight-line basis over the life of the bridge note and initial

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debentures.

The bridge note will mature 15 months from issuance. The principal amount of the bridge note will accrete and compound each month at the rate of 0.833 per cent per month (10 per cent per annum), such that the principal amount at maturity will be \$1,698,843. The bridge note may be repaid by the Company at any time at 101 per cent of the outstanding principal amount, including accreted principal, upon 30 days notice.

In connection with the bridge note, the Company issued to Imperium a five year-term warrant to purchase up to 943,576 share of the Company's common stock at an exercise price of \$0.45 per share. The convertible debenture totaling \$5,000,000 is available in two separate tranches. At the closing, Imperium purchased the initial convertible debenture from the Company for an issuance purchase price of \$3,000,000 in principal amount, which debenture will have a repayment amount of \$3,314,139. On or 24 June 2008, Imperium purchased a \$2,000,000 principal amount convertible debenture from the Company, which will have a repayment amount of \$2,209,426. The initial principal amounts of the debentures will accrete and compound each month at the rate of 0.833 per cent per month (10 per cent per annum) for 12 months from their respective dates of issuance. After one year, the outstanding principal amounts will accrue interest at 8 per cent per annum.

The two tranches of the convertible debenture will be identical in all respects other than the issue and amortization dates. They will amortize in 24 equal monthly payments beginning 3 years from the date of their respective issuance. If the debentures are partially converted, the monthly amortization payments will be reduced proportionately. The Company does not have the ability to call the debenture prior to its maturity. As of 30 June 2008, no amount of the notes had been converted or called.

Imperium may call the debentures upon a change in control of the Company, including a sale of 50 per cent or more of its assets or a merger in which the pre-merger Company stockholders do not hold at least 75 per cent of the surviving entity, and certain other mergers of the Company, or an event of default by the Company under the debentures. In the event of such a call, the Company would be required to repay Imperium the greater of (a) 120 per cent of the unpaid principal amount of the debentures being redeemed plus all accrued and unpaid interest thereon, or (b) an amount calculated pursuant to a formula based upon the Company's stock price at the time of such call. Imperium also may call the bridge note upon a change of control of the Company or an event of default; in such case the Company would be required to repay 101 per cent of the then-outstanding principal plus accrued interest and default interest, under the bridge note. Since the call would double Imperium's initial rate of return on the debentures, the settlement feature is considered an embedded derivative under SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" and has been bifurcated from the convertible debenture and recorded at its estimated fair market value of \$363,298 and \$749,757 at 31 December 2007 and 30 June 2008, respectively. Changes in fair value of the derivative are recorded as interest expense and the difference between face value of the convertible notes and the amount remaining after the bifurcation is recorded as a discount to be amortized over the term of the notes, which is five years.

Payment of the note and debentures is secured by a security interest in the assets of the Company, except certain excluded intellectual property assets.

The principal of the two tranches of the debentures will be convertible at any time at the option of Imperium into common stock of the Company at a price per share of \$0.47 per share. The conversion price was based upon 125 per cent of the average of the 20 daily volume weighted average price per share of the Company's common stock for each of the 20 business days prior to the closing of the initial debenture. The Company will not have the ability to require or force Imperium to convert the debentures. Imperium may not convert if such conversion would result in Imperium holding more than 9.9 per cent of the Company's then-outstanding share of common stock.

The debt financing agreement contains certain covenants pertaining to liquid assets, net working capital and quarterly operating income, as defined in the debt financing agreement. If the Company does not meet the liquid asset or net working capital covenants, Imperium shall have the option to notify the Company in writing demanding the Company prepay the bridge note and/or the convertible debenture then-outstanding by an aggregate amount equal to such shortfall. If the Company does not meet the quarterly operating income covenant, Imperium may call the debentures, as noted above, due to an even of default. The Company is in compliance with all covenants as of 30 June 2008.

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Equipment Financing

In January 2008, the Company entered into an equipment lease line to borrow up to \$1,000,000 at 11.5 per cent per annum to finance the purchase of capital equipment. The outstanding amounts under this arrangement will become due and payable ratably over 10 quarters from the date of each loan schedule. As of 30 June 2008, \$229,506 was outstanding under this arrangement.

NOTE 7 – WARRANTS

In conjunction with a Loan and Security Agreement entered into in March 2004, the Company issued warrants to purchase 200,000 shares of Series C redeemable convertible preferred stock at \$2.50 per share. The warrants expire on 29 March 2011. Using the Black-Scholes option pricing model with a term of seven years, volatility of 70 per cent, no dividend yield and risk-free interest rate of 3.55 per cent., the Company determined that the fair value of the warrant was \$322,000 at the date of issuance, which was recorded as a discount to the notes payable and amortized to interest expense over the loan term. The loan was repaid in full and the discount was taken into interest expense during 2006.

As of 6 April 2006 the warrants were converted from preferred warrants to common warrants. After conversion the warrants are exercisable for an aggregate of 269,803 common shares, at an exercise price of \$1.85 per common share. As of 30 June 2008, all the warrants were outstanding.

In conjunction with the debt financing agreement dated 21 December 2007 (see Note 6), the Company issued warrants to purchase 943,576 share of the Company's common stock at exercise price of \$0.45 per share. The warrants expire 21 December 2012. Using the Black-Scholes option pricing model with a term of five years, volatility of 55 per cent, no dividend yield and risk-free interest rate of 3.58 per cent., the Company determined that the fair value of the warrant was \$191,549 at the date of issuance, which was recorded as a discount to the notes payable and is amortized to interest expense over the loan term. As of 30 June 2008, all the warrants were outstanding.