UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2007

OR

o **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 0-32501

CYTORI THERAPEUTICS, INC.

(Exact name of Registrant as Specified in Its Charter)

DELAWARE	**33-0827593**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
3020 CALLAN ROAD, SAN DIEGO, CALIFORNIA	**92121**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: **(858) 458-0900**

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 ("the Exchange Act") 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 o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act. Large Accelerated Filer o Accelerated Filer o Non-Accelerated Filer ☒

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

As of July 31, 2007, there were 23,918,257 shares of the registrant's common stock outstanding.

CYTORI THERAPEUTICS, INC.

INDEX

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Cytori Therapeutics, Inc.:

We have reviewed the accompanying consolidated condensed balance sheet of Cytori Therapeutics, Inc. and subsidiaries (the Company) as of June 30, 2007, the related consolidated condensed statements of operations and comprehensive loss for the three-month and six-month periods ended June 30, 2007 and 2006, and the consolidated condensed statements of cash flows for the six-month periods ended June 30, 2007 and 2006. These consolidated condensed financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States of America). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the consolidated condensed financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Cytori Therapeutics, Inc. and subsidiaries as of December 31, 2006, and the related consolidated statements of operations and comprehensive loss, stockholders' deficit, and cash flows for the year then ended (not presented herein); and in our report dated March 29, 2007, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated condensed balance sheet as of December 31, 2006, is fairly stated in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ KPMG LLP
San Diego, California
August 8, 2007

CYTORI THERAPEUTICS, INC.
CONSOLIDATED CONDENSED BALANCE SHEETS

	As of June 30, 2007 (unaudited)	As of December 31, 2006
Assets		
Current assets:		
Cash and cash equivalents	$ 22,808,000	$ 8,902,000
Short-term investments, available-for-sale	3,795,000	3,976,000
Accounts receivable, net of allowance for doubtful accounts of $3,000 and $2,000 in 2007 and 2006, respectively	45,000	225,000
Inventories, net	92,000	164,000
Other current assets	564,000	711,000
Total current assets	27,304,000	13,978,000
Property and equipment held for sale, net	—	457,000
Property and equipment, net	3,897,000	4,242,000
Investment in joint venture	82,000	76,000
Other assets	417,000	428,000
Intangibles, net	1,189,000	1,300,000
Goodwill	3,922,000	4,387,000
Total assets	$ 36,811,000	$ 24,868,000
Liabilities and Stockholders' Equity (Deficit)		
Current liabilities:		
Accounts payable and accrued expenses	$ 4,827,000	$ 5,587,000
Current portion of long-term obligations	771,000	999,000
Total current liabilities	5,598,000	6,586,000
Deferred revenues, related party	22,110,000	23,906,000
Deferred revenues	2,379,000	2,389,000
Option liability	1,000,000	900,000
Long-term deferred rent	611,000	741,000
Long-term obligations, less current portion	613,000	1,159,000
Total liabilities	32,311,000	35,681,000
Commitments and contingencies	—	—
Stockholders' equity (deficit):		
Preferred stock, $0.001 par value; 5,000,000 shares authorized; (-0-) shares issued and outstanding in 2007 and 2006	—	—
Common stock, $0.001 par value; 95,000,000 shares authorized; 25,428,778 and 21,612,243 shares issued and 22,555,944 and 18,739,409 shares outstanding in 2007 and 2006, respectively	26,000	22,000
Additional paid-in capital	127,393,000	103,053,000
Accumulated deficit	(116,125,000)	(103,460,000)
Treasury stock, at cost	(6,794,000)	(10,414,000)
Accumulated other comprehensive income	—	1,000
Amount due from exercises of stock options	—	(15,000)
Total stockholders' equity (deficit)	4,500,000	(10,813,000)
Total liabilities and stockholders' equity (deficit)	$ 36,811,000	$ 24,868,000

SEE NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

CYTORI THERAPEUTICS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(UNAUDITED)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2007	2006	2007	2006
Product revenues	$ 512,000	$ 453,000	$ 792,000	$ 955,000
Cost of product revenues	197,000	504,000	422,000	958,000
Gross profit (loss)	315,000	(51,000)	370,000	(3,000)
Development revenues:				
Development, related party	1,796,000	—	1,796,000	683,000
Development	10,000	6,000	10,000	148,000
Research grant and other	8,000	57,000	53,000	63,000
	1,814,000	63,000	1,859,000	894,000
Operating expenses:				
Research and development	4,393,000	6,021,000	9,390,000	11,197,000
Sales and marketing	519,000	473,000	1,065,000	974,000
General and administrative	3,433,000	3,608,000	6,599,000	6,824,000
Change in fair value of option liabilities	(100,000)	(2,665,000)	100,000	(3,140,000)
Total operating expenses	8,245,000	7,437,000	17,154,000	15,855,000
Operating loss	(6,116,000)	(7,425,000)	(14,925,000)	(14,964,000)
Other income (expense):				
Gain on sale of assets	1,858,000	—	1,858,000	—
Interest income	348,000	183,000	545,000	379,000
Interest expense	(43,000)	(53,000)	(95,000)	(111,000)
Other expense, net	(52,000)	(1,000)	(54,000)	(6,000)
Equity gain (loss) from investment in joint venture	9,000	(17,000)	6,000	(66,000)
Total other income (expense)	2,120,000	112,000	2,260,000	196,000
Net loss	(3,996,000)	(7,313,000)	(12,665,000)	(14,768,000)
Other comprehensive loss- unrealized holding loss	—	(10,000)	(1,000)	(24,000)
Comprehensive loss	$ (3,996,000)	$ (7,323,000)	$ (12,666,000)	$ (14,792,000)
Basic and diluted net loss per common share	$ (0.17)	$ (0.47)	$ (0.58)	$ (0.95)
Basic and diluted weighted average common shares	23,497,375	15,592,293	21,790,048	15,510,586

SEE NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

CYTORI THERAPEUTICS, INC.
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	For the Six Months Ended June 30,	
	2007	**2006**
Cash flows from operating activities:		
Net loss	$ (12,665,000)	$ (14,768,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	843,000	1,124,000
Inventory provision	—	70,000
Warranty provision	(43,000)	—
Increase (reduction) in allowance for doubtful accounts	1,000	(5,000)
Change in fair value of option liabilities	100,000	(3,140,000)
Stock-based compensation expense	1,155,000	1,873,000
Gain on sale of assets	(1,858,000)	—
Equity (gain) loss from investment in joint venture	(6,000)	66,000
Increases (decreases) in cash caused by changes in operating assets and liabilities:		
Accounts receivable	179,000	477,000
Inventories	(22,000)	(14,000)
Other current assets	145,000	(170,000)
Other assets	11,000	(63,000)
Accounts payable and accrued expenses	(913,000)	(1,631,000)
Deferred revenues, related party	(1,796,000)	11,817,000
Deferred revenues	(10,000)	(148,000)
Long-term deferred rent	(130,000)	324,000
Net cash used in operating activities	(15,009,000)	(4,188,000)
Cash flows from investing activities:		
Proceeds from sale and maturity of short-term investments	18,459,000	33,222,000
Purchases of short-term investments	(18,280,000)	(32,372,000)
Proceeds from sale of assets	3,175,000	—
Costs from sale of assets	(109,000)	—
Purchases of property and equipment	(365,000)	(2,331,000)
Investment in joint venture	—	(150,000)
Net cash provided by (used in) investing activities	2,880,000	(1,631,000)
Cash flows from financing activities:		
Principal payments on long-term obligations	(774,000)	(460,000)
Proceeds from exercise of employee stock options	908,000	651,000
Proceeds from sale of common stock and warrants	21,500,000	—
Costs from sale of common stock and warrants	(1,599,000)	—
Proceeds from sale of treasury stock	6,000,000	—
Net cash provided by financing activities	26,035,000	191,000
Net increase (decrease) in cash and cash equivalents	13,906,000	(5,628,000)
Cash and cash equivalents at beginning of period	8,902,000	8,007,000
Cash and cash equivalents at end of period	$ 22,808,000	$ 2,379,000
Supplemental disclosure of cash flows information:		
Cash paid during period for:		
Interest	$ 96,000	$ 111,000
Taxes	2,000	1,000
Supplemental schedule of non-cash investing and financing activities:		
Additions to leasehold improvements included in accounts payable and accrued expenses	$ —	$ 287,000

SEE NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

CYTORI THERAPEUTICS, INC.
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS
JUNE 30, 2007
(UNAUDITED)

1. Basis of Presentation

Our accompanying unaudited consolidated condensed financial statements as of June 30, 2007 and for the six months ended June 30, 2007 and 2006 have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for annual financial statements. Our consolidated condensed balance sheet at December 31, 2006 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the financial position and results of operations of Cytori Therapeutics, Inc., and our subsidiaries, have been included. Operating results for the three and six months ended June 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. For further information, refer to our consolidated financial statements for the year ended December 31, 2006 and footnotes thereto which were included in our Annual Report on Form 10-K, dated April 2, 2007.

2. Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America of America requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates. Estimates and assumptions are reviewed periodically, and the effects of revisions are reflected in the consolidated financial statements in the periods they are determined to be necessary.

Our most significant estimates and critical accounting policies involve recognizing revenue, evaluating goodwill for impairment, accounting for product line dispositions, valuing the Put option (see note 12), determining the assumptions used in measuring share-based compensation expense, valuing our deferred tax assets, and assessing how to report our investment in Olympus-Cytori, Inc.

3. Segment Information

We operate as two distinct operating segments - (a) Regenerative cell technology and (b) MacroPore Biosurgery, which manufactures bioresorbable implants. In the past, our resources were managed on a consolidated basis. However, in an effort to better reflect our focus and significant progress in the development of regenerative therapies, we evaluate and report our financial results in two segments.

Our regenerative cell technology segment is developing and seeks to commercialize regenerative cell therapies for cardiovascular disease, reconstructive surgery, and many other serious, chronic, and life-threatening conditions and disorders. We plan to commercialize these therapies through the sale of the Celution™ System, a device that quickly removes regenerative cells from a patient's own adipose tissue, and its related single-use consumables.

Our MacroPore Biosurgery unit manufactured and distributed the HYDROSORB™ family of bioresorbable spine and orthopedic implants, which have been cleared by the Food & Drug Administration ("FDA"); it also develops Thin Film bioresorbable implants for sale in Japan through Senko Medical Trading Company ("Senko"), which has exclusive distribution rights to these products in Japan. We sold the bioresorbable spine and orthopedic implant product line in May 2007 to Kensey Nash Corporation ("Kensey Nash") (see note 14).

We measure the success of each operating segment based on operating profits and losses and, additionally, in the case of the regenerative cell technology segment, the achievement of key research objectives. In arriving at our operating results for each segment, we use the same accounting policies as those used for our consolidated company and as described throughout this note. However, segment operating results exclude allocations of company-wide general and administrative costs and changes in fair value of our option liabilities.

The following tables provide information regarding the performance and assets of our operating segments:

	For the three months ended June 30,		For the six months ended June 30,	
	2007	2006	2007	2006
Revenues:				
Regenerative cell technology	$ 1,804,000	$ 57,000	$ 1,849,000	$ 746,000
MacroPore Biosurgery	522,000	459,000	802,000	1,103,000
Total Revenues	$ 2,326,000	$ 516,000	$ 2,651,000	$ 1,849,000
Segment gains (losses):				
Regenerative cell technology	$ (3,014,000)	$ (6,046,000)	$ (8,364,000)	$ (10,515,000)
MacroPore Biosurgery	231,000	(436,000)	138,000	(765,000)
General and administrative expenses	(3,433,000)	(3,608,000)	(6,599,000)	(6,824,000)
Change in fair value of option liabilities	100,000	2,665,000	(100,000)	3,140,000
Total operating loss	$ (6,116,000)	$ (7,425,000)	$ (14,925,000)	$ (14,964,000)

	As of	As of

	June 30, 2007	December 31, 2006
Assets:		
Regenerative cell technology	$ 28,757,000	$ 9,792,000
MacroPore Biosurgery	92,000	1,758,000
Corporate assets	7,962,000	13,318,000
Total assets	$ 36,811,000	$ 24,868,000

4. Short-Term Investments

We invest excess cash in highly liquid debt instruments of financial institutions and corporations with strong credit ratings and in United States of America government obligations. We have established guidelines relative to diversification and maturities that maintain safety and liquidity. These guidelines are periodically reviewed and modified to take advantage of trends in yields and interest rates.

We evaluate our investments in accordance with the provisions of Statement of Financial Standards ("SFAS") No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Based on our intent, our investment policies, and our ability to liquidate debt securities, we classify short-term investment securities within current assets. Available-for-sale securities are carried at fair value, with unrealized gains and losses reported as accumulated other comprehensive income (loss) within stockholders' equity. The amortized cost basis of debt securities is periodically adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization is included as a component of interest income or interest expense. The amortized cost basis of securities sold is based on the specific identification method and all such realized gains and losses are recorded as a component within other income (expense). Based on such evaluation, management has determined that all investment securities (other than those classified as cash equivalents) are properly classified as available-for-sale.

We review the carrying values of our investments and write down such investments to estimated fair value by a charge to the statements of operations when the severity and duration of a decline in the value of an investment is considered to be other than temporary. The cost of securities sold or purchased is recorded on the trade date.

At June 30, 2007, the excess of carrying cost over the fair value of our short-term investments is immaterial.

5. Summary of Significant Accounting Policies

Inventories

Inventories include the cost of material, labor, and overhead, and are stated at the lower of average cost, determined on the first-in, first-out (FIFO) method, or market. We periodically evaluate our on-hand stock and make appropriate provisions for any stock deemed excess or obsolete. We expense excess manufacturing costs, that is, costs resulting from lower than "normal" production levels.

During the second quarter of 2006, we recorded a provision of $70,000 for excess raw materials that we determined were unlikely to be converted into finished goods and ultimately sold. No inventory provisions were recorded during the first six months of 2007.

See note 14 for a description of the sale of our bioresorbable spine and orthopedic implant product line.

Property and Equipment

Property and equipment is stated at cost, net of accumulated depreciation. Depreciation expense is provided for on a straight-line basis over the estimated useful lives of the assets, or the life of the lease (as applicable), whichever is shorter, and range from three to seven years. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is included in operations. Maintenance and repairs are charged to operations as incurred.

Revenue Recognition

Product Sales

Before the disposal of our bioresorbable spine and orthopedic product line in May 2007, we sold our (non-Thin Film) MacroPore Biosurgery products to Medtronic, Inc. under a Distribution Agreement dated January 5, 2000 and amended December 22, 2000 and October 8, 2002, as well as a Development and Supply Agreement dated January 5, 2000 and amended December 22, 2000 and September 30, 2002. These revenues are classified as product revenues in our statements of operations.

We recognized revenue on product sales to Medtronic only after both (a) the receipt of a purchase order from Medtronic and (b) shipment of ordered products to Medtronic, as title and risk of loss pass upon shipment.

In the past, we would offer Medtronic extended payment terms. In these circumstances, we did not recognize revenues under these arrangements until the payment became due or was received, if that occurred earlier. Moreover, we warranted that our products were free from manufacturing defects at the time of shipment. We have recorded a reserve for the estimated costs we may incur under our warranty program for products previously sold.

License/Distribution Fees

If separable under Emerging Issues Task Force Issue 00-21, "Revenue Arrangements with Multiple Deliverables" ("EITF 00-21"), we recognize any upfront payments received from license/distribution agreements as revenues ratably over the period in which the customer benefits from the license/distribution agreement.

To date, we have not received any upfront license payments that are separable under EITF 00-21. Accordingly, such license revenues have been combined with other elements, such as research and development activities, for purposes of revenue recognition. For instance, we account for the license fees and milestone payments under the Distribution Agreement with Senko as a single unit of accounting. Similarly, we have attributed the upfront fees received under the arrangements with Olympus Corporation, a related party, to a combined unit of accounting comprising a license we granted to Olympus-Cytori, Inc. (the "Joint Venture"), a related party, as well as development services we agreed to perform for this entity.

In the first quarter of 2006, we granted Olympus an exclusive right to negotiate a commercialization collaboration for the use of adipose regenerative cells for a specific therapeutic area outside of cardiovascular disease. In exchange for this right, we received $1,500,000 from Olympus, which is non-

refundable but may be applied towards any definitive commercial collaboration in the future. As part of this agreement, Olympus will conduct market research and pilot clinical studies in collaboration with us over a 12 to 18 month period for the therapeutic area. The $1,500,000 payment was received in the second quarter of 2006 and recorded as deferred revenues, related party. The deferred revenues, related party, will be recognized as revenue in the statement of operations either (i) in connection with other consideration received as part of a definitive commercial collaboration in the future, or (ii) when the exclusive negotiation period expires.

In the third quarter of 2004, we entered into a Distribution Agreement with Senko. Under this agreement, we granted to Senko an exclusive license to sell and distribute certain Thin Film products in Japan and received a $1,500,000 upfront license fee from them in return for this right. We have recorded the $1,500,000 received as a component of deferred revenues in the accompanying balance sheet. Half of the license fee is refundable if the parties agree commercialization is not achievable and a proportional amount is refundable if we terminate the arrangement, other than for material breach by Senko, before three years post-commercialization.

Research and Development

We earn revenue for performing tasks under research and development agreements with both commercial enterprises, such as Olympus and Senko, and governmental agencies like the National Institutes of Health ("NIH"). Revenue earned under development agreements is classified as either research grant or development revenues in our statements of operations, depending on the nature of the arrangement. The costs associated with earning these revenues are typically recorded as research and development expense.

We received a total of $22,000,000 from Olympus and Olympus-Cytori, Inc. during 2005 in two separate but related transactions (see note 12). Approximately $4,689,000 of this amount related to common stock that we issued, as well as options we granted, to Olympus. Moreover, during the first quarter of 2006, we received $11,000,000 from the Joint Venture upon achieving the CE Mark on the Celution™ System. Considering the $4,689,000 initially allocated to the common stock issued and the two options, we recorded upfront fees totaling $28,311,000 as deferred revenues, related party. In exchange for these proceeds, we agreed to (a) provide Olympus-Cytori, Inc. an exclusive and perpetual license to our therapeutic device technology, including the Celution™ System and certain related intellectual property, and (b) perform future development services related to commercializing the Celution™ System (see note 12). As noted above, the license and development services are not separable under EITF 00-21. Accordingly, we will recognize the $28,311,000 allocated to deferred revenues, related party, using a proportional performance methodology- that is, as we complete substantive milestones related to the development component of the combined accounting unit. As of June 30, 2007, we have recognized $7,701,000 of the deferred revenues, related party as development revenues of which $1,796,000 was recognized in the three and six months ended June 30, 2007. All related development costs are expensed as incurred and are included in research and development expense on the statement of operations.

In the third quarter of 2004, we entered into a Distribution Agreement with Senko. Under this agreement, we granted to Senko an exclusive license to sell and distribute certain Thin Film products in Japan. We have also earned or will be entitled to earn additional payments under the Distribution Agreement based on achieving the following defined research and development milestones:

- In 2004, we received a non-refundable payment of $1,250,000 from Senko after filing an initial regulatory application with the Japanese Ministry of Health, Labour and Welfare ("MHLW") related to the Thin Film product line. We initially recorded this payment as deferred revenues of $1,250,000.

- Upon the achievement of commercialization (i.e., regulatory approval by the MHLW), we will be entitled to an additional nonrefundable payment of $250,000.

Of the amounts received and deferred, we recognized development revenues of $10,000 and $148,000 in the six months ended June 30, 2007 and 2006, respectively, representing the fair value of the completed milestones relative to the fair value of the total efforts expected to be necessary to achieve regulatory approval by the MHLW. As noted above, the license and the milestone components of the Senko Distribution Agreement are accounted for as a single unit of accounting. This single element includes a $1,500,000 license fee which is potentially refundable. We have recognized, and will continue to recognize, the non-contingent fees allocated to this combined deliverable as we complete performance obligations under the Distribution Agreement with Senko. Accordingly, we expect to recognize approximately $1,129,000 (consisting of the remaining $879,000 in deferred revenues plus a non-refundable payment of $250,000 to be received upon commercialization) in revenues associated with this milestone arrangement once commercialization is achieved. We will not recognize the potentially refundable portion of the fees until the right of refund expires.

6. Long-Lived Assets

In accordance with SFAS No. 144, "Accounting for Impairment or Disposal of Long-Lived Assets," we assess certain long-lived assets, such as property and equipment and intangible assets other than goodwill, for potential impairment when there is a change in circumstances that indicates carrying values of assets may not be recoverable. Such long-lived assets are deemed to be impaired when the undiscounted cash flows expected to be generated by the asset (or asset group) are less than the asset's carrying amount. Any required impairment loss would be measured as the amount by which the asset's carrying value exceeds its fair value, and would be recorded as a reduction in the carrying value of the related asset and a charge to operating expense. During the six months ended June 30, 2007 and 2006, we had no impairment losses associated with our long-lived assets.

7. Share-Based Compensation

During the first quarter of 2007, we issued to our officers and directors stock options to purchase up to 410,000 shares of our common stock, with a four-year vesting for our officers and 24-month vesting for our directors. The grant date fair value of option awards granted to our officers and directors was $3.82 and $3.70 per share, respectively. The resulting share-based compensation expense of $1,480,000, net of estimated forfeitures, will be recognized as expense over the respective vesting periods.

During the second quarter of 2007, we made a company-wide option grant to our non-executive employees to purchase up to 213,778 shares of our common stock, subject to a four-year vesting schedule. The grant date fair value for the awards was $3.66. The resulting share-based compensation expense of $739,000, net of estimated forfeitures, will be recognized as expense over the respective vesting periods.

8. Income Taxes

On July 13, 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48 ("FIN 48"), "Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109." FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109 ("SFAS 109"), "Accounting for Income Taxes," and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Under FIN 48, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006.

We adopted the provisions of FIN 48 on January 1, 2007. There were no unrecognized tax benefits as of the date of adoption. There are no unrecognized tax benefits included in the balance sheet that would, if recognized, affect the effective tax rate.

Our practice is to recognize interest and/or penalties related to income tax matters in income tax expense. We had $0 accrued for interest and penalties on our balance sheet as of June 30, 2007 and December 31, 2006, and have recognized $0 in interest and/or penalties in our statement of operations for the three and six months ended June 30, 2007.

With limited exception, we are subject to taxation in the U.S. and California jurisdictions. Our tax years for 1997 and forward are subject to examination by the U.S. and California tax authorities due to the carryforward of unutilized net operating losses and research and development credits.

The adoption of FIN No. 48 did not impact our financial condition, results of operations, or cash flows. At January 1, 2007, we had net deferred tax assets of $38,505,000. The deferred tax assets are primarily composed of federal and state tax net operating loss carryforwards and federal and state research and development ("R&D") credit carryforwards. Due to uncertainties surrounding our ability to generate future taxable income to realize these assets, a full valuation allowance has been established to offset our deferred tax assets. Additionally, the future utilization of our net operating loss and R&D credit carryforwards to offset future taxable income may be subject to a substantial annual limitation as a result of ownership changes that may have occurred previously or that could occur in the future. We are in the process of updating our Section 382/383 analysis through the period ending December 31, 2006. We have not yet determined whether such an ownership change has occurred, however, the Company is currently working to complete a Section 382/383 analysis regarding the limitation of the net operating losses and research and development credits. Similarly, we plan to complete an R&D credit analysis regarding the calculation of the R&D credit. When these analyses are completed, we may need to update the amount of unrecognized tax benefits we have reported under FIN No. 48. Therefore, we expect that the unrecognized tax benefits may change within 12 months of this reporting date. At this time, we cannot estimate how much the unrecognized tax benefits may change. Due to the existence of the valuation allowance, future changes in our unrecognized tax benefits will not impact our effective tax rate.

9. Loss per Share

We compute loss per share based on the provisions of SFAS No. 128, “Earnings per Share.” Basic per share data is computed by dividing net income or loss available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted per share data is computed by dividing net income or loss available to common stockholders by the weighted average number of common shares outstanding during the period increased to include, if dilutive, the number of additional common share equivalents that would have been outstanding if potential common shares had been issued using the treasury stock method. Potential common shares were related entirely to outstanding but unexercised options and warrants for all periods presented.

We have excluded all potentially dilutive securities from the calculation of diluted loss per share attributable to common stockholders for the three and six months ended June 30, 2007 and 2006, as their inclusion would be antidilutive. Potentially dilutive common shares excluded from the calculations of diluted loss per share were 8,161,043 and 8,344,536 for the three and six months ended June 30, 2007 and 2006, respectively.

10. Commitments and Contingencies

We have entered into agreements, which have provisions for cancellation, with various clinical research organizations for pre-clinical and clinical development studies. Under the terms of these agreements, the vendors provide a variety of services including conducting pre-clinical development research, enrolling patients, recruiting patients, monitoring studies, and data analysis. Payments under these agreements typically include fees for services and reimbursement of expenses. The timing of payments due under these agreements is estimated based on current schedules of pre-clinical and clinical studies in progress. As of June 30, 2007, we have pre-clinical research study obligations of $267,000 (all of which are expected to be completed within a year) and clinical research study obligations of $6,314,000 ($5,458,000 of which are expected to be completed within a year).

We are subject to various claims and contingencies related to legal proceedings. Due to their nature, such legal proceedings involve inherent uncertainties including, but not limited to, court rulings, negotiations between affected parties, and governmental actions. Management assesses the probability of loss for such contingencies and accrues a liability and/or discloses the relevant circumstances, as appropriate. Management believes that any liability to us that may arise as a result of currently pending legal proceedings will not have a material adverse effect on our financial condition, liquidity, or results of operations as a whole.

Refer to note 11 for a discussion of our commitments and contingencies related to our interactions with the University of California.

Refer to note 12 for a discussion of our commitments and contingencies related to our transactions with Olympus, including (a) our obligation to the Joint Venture in future periods and (b) certain put and call rights embedded in the arrangements with Olympus.

11. License Agreement

On October 16, 2001, StemSource, Inc. entered into an exclusive worldwide license agreement with the Regents of the University of California (“UC”), licensing all of UC’s rights to certain pending patent applications being prosecuted by UC and (in part) by the University of Pittsburgh, for the life of these patents, with the right of sublicense. The exclusive license relates to an issued patent (“Patent 6,777,231”) and various pending applications relating to adipose-derived stem cells. In November 2002, we acquired StemSource, and the license agreement was assigned to us.

The agreement, which was amended and restated in September 2006 to better reflect our business model, calls for various periodic payments until such time as we begin commercial sales of any products utilizing the licensed technology. Upon achieving commercial sales of products or services covered by the UC license agreement, we will be required to pay variable earned royalties based on the net sales of products sold. Minimum royalty amounts will increase annually with a plateau in 2015. In addition, there are certain due diligence milestones that are required to be reached as a result of the agreement. Failure to fulfill these milestones may result in a reduction of or loss of the specific rights to which the effected milestone relates.

In connection with the amendment of the agreement in the third quarter of 2006, we agreed to issue 100,000 shares of our common stock to UC in the fourth quarter of 2006. At the time the agreement was reached, our shares were trading at $4.87 per share. The expense was charged to general and administrative expense.

Additionally, we are obligated to reimburse UC for patent prosecution and other legal costs on any patent applications contemplated by the agreement. In particular, the University of Pittsburgh filed a lawsuit in the fourth quarter of 2004, naming all of the inventors who had not assigned their ownership interest in Patent 6,777,231 to the University of Pittsburgh. It was seeking a determination that its assignors, rather than UC’s assignors, are the true inventors of Patent 6,777,231. This lawsuit has subjected us to and could continue to subject us to significant costs and, if the University of Pittsburgh wins the lawsuit, our license rights to this patent could be nullified or rendered non-exclusive with respect to any third party that might license rights from the University of Pittsburgh.

We are not named as a party to the lawsuit, but our president, Marc Hedrick, is one of the inventors identified on the patent and therefore is a named individual defendant. We are providing substantial financial and other assistance to the defense of the lawsuit.

In the three and six months ended June 30, 2007, we expensed $518,000 and $602,000, respectively, for legal fees related to this license. For the same periods in 2006, we expensed $861,000 and $1,366,000, respectively. These expenses have been classified as general and administrative expense in the accompanying financial statements. We believe that the amount accrued as of June 30, 2007 is a reasonable estimate of our liability for the expenses incurred to date.

12. Transactions with Olympus Corporation

Initial Investment by Olympus Corporation in Cytori

In the second quarter of 2005, we entered into a Common Stock Purchase Agreement (the “Purchase Agreement”) with Olympus under which we received $11,000,000 in cash proceeds.

Under this agreement, we issued 1,100,000 newly issued shares of common stock to Olympus. In addition, we also granted Olympus an immediately exercisable option to acquire 2,200,000 shares of our common stock at $10 per share, which expired on December 31, 2006. Before its expiration, we accounted for this grant as a liability in accordance with EITF 00-19, “Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company’s Own Stock” because from the date of grant through the expiration, we would have been required to deliver listed common stock to settle the option shares upon exercise.

The $11,000,000 in total proceeds we received in the second quarter of 2005 exceeded the sum of (i) the market value of our stock as well as (ii) the fair value of the option at the time we entered into the share purchase agreement. The $7,811,000 difference between the proceeds received and the fair values of our common stock and option liability is recorded as a component of deferred revenues, related party, in the accompanying balance sheet.

In August 2006, we received an additional $11,000,000 from Olympus for the issuance of approximately 1,900,000 shares of our common stock at $5.75 per share under the shelf registration statement filed in May 2006. The purchase price was determined by our closing price on August 9, 2006.

As of June 30, 2007, Olympus holds approximately 12.7% of our issued and outstanding shares. Additionally, Olympus has a right, which it has not yet exercised, to designate a director to serve on our Board of Directors.

Formation of the Olympus-Cytori Joint Venture

On November 4, 2005, we entered into a joint venture and other related agreements (the "Joint Venture Agreements") with Olympus. The Joint Venture is owned equally by Olympus and us.

Under the Joint Venture Agreements:

- Olympus paid $30,000,000 for its 50% interest in the Joint Venture. Moreover, Olympus simultaneously entered into a License/Joint Development Agreement with the Joint Venture and us to develop a second generation commercial system and manufacturing capabilities.

- We licensed our device technology, including the Celution™ System and certain related intellectual property, to the Joint Venture for use in future generation devices. These devices will process and purify regenerative cells residing in adipose tissue for various therapeutic clinical applications. In exchange for this license, we received a 50% interest in the Joint Venture, as well as an initial $11,000,000 payment from the Joint Venture; the source of this payment was the $30,000,000 contributed to the Joint Venture by Olympus. Moreover, upon receipt of a CE Mark for the first generation Celution™ System in January 2006, we received an additional $11,000,000 development milestone payment from the Joint Venture.

We have determined that the Joint Venture is a variable interest entity ("VIE") pursuant to FASB Interpretation No. 46 (revised 2003), "Consolidation of Variable Interest Entities - An Interpretation of ARB No. 51" ("FIN 46R"), but that Cytori is not the VIE's primary beneficiary. Accordingly, we have accounted for our interests in the Joint Venture using the equity method of accounting, since we can exert significant influence over the Joint Venture's operations. At June 30, 2007, the carrying value of our investment in the Joint Venture is $82,000.

We are under no obligation to provide additional funding to the Joint Venture, but may choose to do so. In the first quarter of 2006, we contributed $150,000 to the Joint Venture.

Put/Calls and Guarantees

The Shareholders' Agreement between Cytori and Olympus provides that in certain specified circumstances of insolvency or if we experience a change in control, Olympus will have the rights to (i) purchase our interests in the Joint Venture at the fair value of such interests or (ii) sell its own interests in the Joint Venture to Cytori at the higher of (a) $22,000,000 or (b) the Put's fair value.

As of November 4, 2005, the fair value of the Put was determined to be $1,500,000. At June 30, 2007 and December 31, 2006, the fair value of the Put was $1,000,000 and $900,000, respectively. Fluctuations in the Put value are recorded in the statements of operations as a component of change in fair value of option liabilities. The Put itself, which is perpetual, has been recorded as a long-term liability in the caption Option liability in the balance sheet.

The valuations of the Put were completed by an independent valuation firm using an option pricing theory-based simulation analysis (i.e., a Monte Carlo simulation). The valuations are based on assumptions as of the valuation date with regard to the market value of Cytori and the estimated fair value of the Joint Venture, the expected correlation between the values of Cytori and the Joint Venture, the expected volatility of Cytori and the Joint Venture, the bankruptcy recovery rate for Cytori, the bankruptcy threshold for Cytori, the probability of a change of control event for Cytori, and the risk-free interest rate.

The following assumptions were employed in estimating the value of the Put:

	June 30, 2007	December 31, 2006	November 4, 2005
Expected volatility of Cytori	61.00%	66.00%	63.20%
Expected volatility of the Joint Venture	61.00%	56.60%	69.10%
Bankruptcy recovery rate for Cytori	21.00%	21.00%	21.00%
Bankruptcy threshold for Cytori	$ 10,460,000	$ 10,110,000	$ 10,780,000
Probability of a change of control event for Cytori	2.22%	1.94%	3.04%
Expected correlation between fair values of Cytori and the Joint Venture in the future	99.00%	99.00%	99.00%
Risk-free interest rate	5.03%	4.71%	4.66%

The Put has no expiration date. Accordingly, we will continue to recognize a liability for the Put and mark it to market each quarter until it is exercised or until the arrangements with Olympus are amended.

Olympus-Cytori Joint Venture

The Joint Venture has exclusive access to our technology for the development, manufacture, and supply of the devices (second generation and beyond) for all therapeutic applications. Once a second generation Celution™ System is developed and approved by regulatory agencies, the Joint Venture may sell such systems exclusively to us at a formula-based transfer price; we have retained marketing rights to the second generation devices for all therapeutic applications of adipose regenerative cells.

As part of the various agreements with Olympus, we will be required, following commercialization of the Celution™ System, to provide monthly forecasts to the Joint Venture specifying the quantities of each category of devices that we intend to purchase over a rolling six-month period. Although we are not subject to any minimum purchase requirements, we are obliged to buy a minimum percentage of the products forecasted by us in such reports. Since we can effectively control the number of devices we will agree to purchase and because no commercial devices have yet been developed to trigger the forecast requirement, we estimate that the fair value of this guarantee is de minimis as of June 30, 2007.

Deferred revenues, related party

As of June 30, 2007, the deferred revenues, related party account primarily consists of the consideration we have received in exchange for future services that we have agreed to perform on behalf of Olympus and the Joint Venture. These services include completing pre-clinical and clinical studies, product development and seeking regulatory approval for the treatment of various therapeutic conditions with regenerative cells residing in adipose tissue. These services also include maintaining the exclusive and perpetual license to our device technology, including the Celution™ System and certain related intellectual property.

Pursuant to EITF 00-21, we have concluded that the license and development services must be accounted for as a single unit of accounting. Refer to note 5 for a full description of our revenue recognition policy.

13. Common Stock

In February 2007, we completed a registered direct public offering of units consisting of common stock and warrants. We received net proceeds of $19,901,000 from the sale of units consisting of 3,746,000 shares of common stock and 1,873,000 common stock warrants (with an exercise price of $6.25 per share and a five-year exercisability period) under our shelf registration statement.

In April 2007, we sold 1,000,000 shares of unregistered common stock out of our treasury stock to Green Hospital Supply, Inc. for $6,000,000 cash. We agreed to seek Securities and Exchange Commission registration of the shares for resale if so requested. The sale agreement contains no registration payment arrangements within the scope of FASB Staff Position EITF 00-19-2.

14. Gain on Sale of Assets, Spine and Orthopedics Product Line

In May 2007, we sold to Kensey Nash our intellectual property rights and tangible assets related to our spine and orthopedic product line, a part of our MacroPore Biosurgery business. Excluded from the sale was our Japan Thin Film product line.

We received $3,175,000 in cash proceeds related to the disposition. The assets comprising the spine and orthopedic product line transferred to Kensey Nash were as follows:

	Carrying Value Prior to Disposition
Inventory	$ 94,000
Other current assets	17,000
Assets held for sale	436,000
Goodwill	465,000
	$ 1,012,000

We incurred expenses of $109,000 in connection with the sale. We recognized approximately $1,858,000 as gain on sale in the statement of operations during the second quarter of 2007.

The revenues and expenses related to the spine and orthopedic product line transferred to Kensey Nash for the three and six months ended June 30, 2007 and 2006 were as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2007	2006	2007	2006
Revenues	$ 512,000	$ 453,000	$ 792,000	$ 955,000
Cost of product revenues	(197,000)	(504,000)	(422,000)	(958,000)
Research & development	(31,000)	(279,000)	(113,000)	(609,000)
Sales & marketing	(8,000)	(50,000)	(21,000)	(138,000)

As part of the disposition agreement, we are required to provide training to Kensey Nash representatives in all aspects of the manufacturing process related to the transferred spine and orthopedic product line, and to act in the capacity of a product manufacturer from the point of sale through August 2007. Because of these additional manufacturing requirements, we deferred $196,000 of the gain related to the outstanding manufacturing requirements to be completed by August 31, 2007.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This report contains certain statements that may be deemed "forward-looking statements" within the meaning of United States of America securities laws. All statements, other than statements of historical fact, that address activities, events or developments that we intend, expect, project, believe or anticipate will or may occur in the future are forward-looking statements. Such statements are based upon certain assumptions and assessments made by our management in light of their experience and their perception of historical trends, current conditions, expected future developments and other factors they believe to be appropriate. The forward-looking statements included in this report are also subject to a number of material risks and uncertainties, including but not limited to the risks described under the "Risk Factors" section in Part II below.

We encourage you to read those descriptions carefully. We caution you not to place undue reliance on the forward-looking statements contained in this report. These statements, like all statements in this report, speak only as of the date of this report (unless an earlier date is indicated) and we undertake no obligation to update or revise the statements except as required by law. Such forward-looking statements are not guarantees of future performance and actual results will likely differ, perhaps materially, from those suggested by such forward-looking statements.

Overview

Regenerative Cell Technology

Cytori is developing the Celution™ System, an innovative medical device that removes patients' regenerative cells from their own fat tissue so that these cells can be delivered to the same patient in about an hour. The commercialization model will be based on the sale of the system and related single-use therapeutic sets that are tailored to each therapeutic application. We are focused initially on bringing applications to market for reconstructive surgery, cardiovascular disease and cell banking. Our success is dependent upon our ability to conduct well-designed clinical trials that demonstrate patient benefit and support reimbursement and physician adoption. We will also need to seek regulatory clearances for the Celution™ System around the world, and build out our commercialization and manufacturing infrastructure.

The following are our major initiatives over the next six to 18 months:

- To initiate a limited market introduction of the Celution™ System in Europe for reconstructive surgery;
- To launch our Celution™ System -based cell preservation product in Japan;
- To advance and expand our clinical development product pipeline; and
- To make continued progress in our corporate partnering efforts.

The major milestones, which will measure our success over this time, are the following:

- Initiation of the APOLLO heart attack safety and feasibility trial;
- Announcement of the outcome of the investigator-initiated breast reconstruction safety study in Japan;
- Initiation of a multi-center breast reconstruction claims expansion and reimbursement trial in Europe;
- Expansion of the Celution™ System distribution network for reconstructive surgery;
- Completion of the internal manufacture build-out for the Celution™ System to meet anticipated product demand in 2008 and early 2009;
- The achievement of commercialization partners for the Celution™ System in select therapeutic areas; and
- The signing of a commercialization agreement for adipose-derived regenerative cell banking in Japan.

Breast Reconstruction

During the first half of 2007, we continued to make progress toward our commercial launch of the Celution™ System. Our goal is to make the Celution™ System available on a targeted basis in Europe in early 2008 for reconstructive surgery. This will be followed by a broader launch in 2009, when we achieve reimbursement for reconstruction of breast tissue following a partial mastectomy (lumpectomy) in breast cancer patients.

To date we have entered distribution agreements for Belgium, Greece, Italy, Luxembourg, Portugal, Spain, and The Netherlands to prepare for the launch of our Celution™ System. We expect to continue to expand our international distribution network for additional countries throughout Europe later this year. In parallel, we are building out our internal manufacturing capabilities so that we will be in a position to meet anticipated demand in 2008 and 2009 until the Olympus-Cytori Joint Venture, described below, is expected to fulfill device manufacturing.

We have made progress toward initiating a clinical trial later this year for the Celution™ System for restoring volume and contour defects resulting from breast conservation therapy in breast cancer patients. The goal of this study is to achieve expanded marketing claims and to support reimbursement for use of adipose-derived regenerative cells, processed via the Celution™ System, in breast reconstruction post-partial mastectomy.

Breast reconstruction in partial mastectomy patients represents an important market for which there are few, if any, available treatment options. In Europe alone, there are an estimated 300,000 patients diagnosed with breast cancer each year of which an estimated 60% are considered eligible for a partial mastectomy. Approximately 3,000,000 women in Europe are already diagnosed with breast cancer. This figure includes women who are newly diagnosed, in active treatment, have completed active treatment, and those living with progressive symptoms of their disease.

Cardiovascular Disease

In January 2007, we initiated a clinical trial of adipose-derived regenerative cells, processed via the Celution™ System, for chronic myocardial ischemia, a severe form of coronary artery disease. It is designed as a 36-patient, double-blind, placebo-controlled, dose-escalation safety and feasibility study. The patients' cells are extracted from their adipose tissue using the Celution™ System, and then injected into the injured oxygen-deprived areas of their hearts through a specially designed catheter. The patients will be evaluated for six months after treatment. The study is being conducted at Gregorio Marañón Hospital in Madrid, Spain and led by Drs. Francisco J. Fernández-Avilés and Emerson Perin. Enrollment for this trial remains on track and results are expected to be reported in the second half of 2008.

We expect to start a clinical trial of adipose-derived regenerative cells, processed via the Celution™ System, in heart attack patients later in 2007. This trial is designed as a 48-patient double-blind, placebo-controlled, dose-escalation safety and feasibility study. The patients' cells will be extracted from their adipose tissue using the Celution™ System and injected into their coronary artery. Once started, the enrollment duration is expected to be 18 months and initial results are to be reported in approximately 27 months.

The American Heart Association estimates that in the United States of America alone, there are approximately 1.2 million heart attacks each year and more than 5.2 million people suffer from a form of chronic heart disease. Given the size of this market and the favorable pre-clinical data demonstrating functional improvement, cardiovascular disease represents a very important application for our Celution™ System and we believe that outcome of the clinical data from these safety and feasibility studies could have a significant impact on our future operations.

Olympus Partnership

On November 4, 2005, we entered into a strategic development and manufacturing joint venture agreement and other related agreements ("JV Agreements") with Olympus Corporation ("Olympus"). As part of the terms of the JV Agreements, we formed a joint venture, Olympus-Cytori, Inc. (the "Joint Venture"), to develop and manufacture future generation devices based on our Celution™ System.

Under the Joint Venture Agreements:

- Olympus paid $30,000,000 for its 50% interest in the Joint Venture. Moreover, Olympus simultaneously entered into a License/Joint Development Agreement with the Joint Venture and us to develop a second generation commercial system and manufacturing capabilities.

- We licensed our device technology, including the Celution™ System and certain related intellectual property, to the Joint Venture for use in future generation devices. These devices will process and purify regenerative cells residing in adipose tissue for various therapeutic clinical applications. In exchange for this license, we received a 50% interest in the Joint Venture, as well as an initial $11,000,000 payment from the Joint Venture; the source of this payment was the $30,000,000 contributed to the Joint Venture by Olympus. Moreover, upon receipt of a CE Mark for the first generation Celution™ System in January 2006, we received an additional $11,000,000 development milestone payment from the Joint Venture.

Put/Calls and Guarantees

The Shareholders' Agreement between Cytori and Olympus provides that in certain specified circumstances of insolvency or if we experience a change in control, Olympus will have the rights to (i) repurchase our interests in the Joint Venture at the fair value of such interests or (ii) sell its own interests in the Joint Venture to Cytori at the higher of (a) $22,000,000 or (b) the Put's fair value.

The Put has no expiration date. Accordingly, we will continue to recognize a liability for the Put and mark it to market each quarter until it is exercised or until the arrangements with Olympus are amended.

Olympus-Cytori Joint Venture

The Joint Venture currently has exclusive access to our technology for the development, manufacture, and supply of the devices (second generation and beyond) for all therapeutic applications. Once a second generation Celution™ System is developed and approved by regulatory agencies, the Joint Venture may sell such systems exclusively to us at a formula-based transfer price; we have retained marketing rights to the second generation devices for all therapeutic applications of adipose regenerative cells.

We have worked closely with Olympus' team of scientists and engineers to design future generations of the Celution™ System that contain certain product enhancements and that can be manufactured in a streamlined manner. For the remainder of 2007, the Joint Venture will continue its efforts with the goal of scale-up manufacturing available in late 2008 or early 2009.

We account for our investment in the Joint Venture under the equity method of accounting.

Other Related-Party Transactions

In a separate agreement entered into on February 23, 2006, we granted Olympus an exclusive right to negotiate a commercialization collaboration for the use of adipose regenerative cells for a specific therapeutic area outside of cardiovascular disease. In exchange for this right, we received a $1.5 million payment from Olympus. As part of this agreement, Olympus will conduct market research and pilot clinical studies in collaboration with us over a 12 to 18 month period for the therapeutic area.

In the third quarter of 2006, we received net proceeds of $16,219,000 from the sale of common stock pursuant to a shelf registration statement, of which $11,000,000 of common stock was purchased by Olympus.

MacroPore Biosurgery

Spine and orthopedic products

We have completed our transition away from the bioresorbable spine and orthopedic surgical implants business for which we were originally founded. We sold our product line to Kensey Nash Corporation ("Kensey Nash") in the second quarter of 2007.

Thin Film Japan Distribution Agreement

In 2004, we sold the majority of our Thin Film business to MAST Biosurgery, AG ("MAST").

Even after consummation of the 2004 Thin Film asset sale to MAST, we retained all rights to Thin Film business in Japan (subject to a purchase option of MAST, which expired in May 2007), and we received back from MAST a license of all rights to Thin Film technologies in the:

- Spinal field, exclusive at least until 2012, and
- Field of regenerative medicine, non-exclusive on a perpetual basis.

In the third quarter of 2004, we entered into a Distribution Agreement with Senko. Under this agreement, we granted to Senko an exclusive license to sell and distribute certain Thin Film products in Japan. Specifically, the license covers Thin Film products with the following indications:

- Anti-adhesion,
- Soft tissue support, and
- Minimization of the attachment of soft tissues.

The Distribution Agreement with Senko commences upon "commercialization." In simplest terms, commercialization occurs when one or more Thin Film product registrations are completed with the Japanese Ministry of Health, Labour and Welfare ("MHLW"). We are currently in the process of seeking approval from the MHLW but commercialization has not yet occurred.

Following commercialization, the Distribution Agreement has a duration of five years and is renewable for an additional five years after reaching mutually agreed minimum purchase guarantees.

We received a $1,500,000 upfront license fee from Senko. We have recorded the $1,500,000 received as a component of deferred revenues in the accompanying balance sheet. Half of the license fee is refundable if the parties agree commercialization is not achievable and a proportional amount is refundable if we terminate the arrangement, other than for material breach by Senko, before three years post-commercialization.

Under the Distribution Agreement, we will also be entitled to earn additional payments from Senko based on achieving defined milestones. On September 28, 2004, we notified Senko of completion of the initial regulatory application to the MHLW for the Thin Film product. As a result, we became entitled to a nonrefundable payment of $1,250,000, which we received in October 2004 and recorded as a component of deferred revenues. We recognized $10,000 during the three and six months ended June 30, 2007. We recognized $6,000 and $148,000 in development revenues during the same periods in 2006, respectively.

Liquidity

As our regenerative cell technology business is still in the development stage and requires large amounts of cash, it is important that we maintain sufficient liquidity to support our future cash needs. As of June 30, 2007, we had cash, cash equivalents, and short-term investments on hand of $26,603,000, which included approximately $19,901,000 that was raised from an equity offering in February 2007, net of fees and expenses. In the second quarter of 2007, we received $6,000,000 from the sale of 1,000,000 shares to Green Hospital Supply, Inc. During the second quarter of 2007, we also received $3,175,000 from the sale of our spine and orthopedic product line to Kensey Nash.

Results of Operations

Our overall net loss for the three and six months ended June 30, 2007 was $3,996,000 and $12,665,000, which was driven by $4,393,000 and $9,390,000 in research and development expenses and $3,433,000 and $6,599,000 in general and administrative expenses, respectively. This compares to a net loss of $7,313,000 and $14,768,000 during the three and six months ended June 30, 2006, respectively. The net loss for the second quarter and six months ended June 30, 2007 reflects expenses related to preparations for regenerative cell technology commercialization, including build-out of our manufacturing capability, as well as costs associated with clinical trials. The losses for these periods were offset in part by the recognition of a gain on the sale of our bioresorbable spine and orthopedic implant product line as well as the recognition of development revenue in the second quarter of 2007. We expect our net operating loss for 2007 will be approximately $25,000,000.

Product revenues

Product revenues in 2007 and 2006 relate to our MacroPore Biosurgery segment and consisted of revenues from our spine and orthopedic products. The following table summarizes the components for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Spine and orthopedics products	$512,000	$453,000	$ 59,000	13.0%	$792,000	$955,000	$ (163,000)	(17.1)%
% attributable to Medtronic	100%	100%			100%	100%		

Spine and orthopedic product revenues represent sales of bioresorbable implants used in spine and orthopedic surgical procedures. We sold this line of business to Kensey Nash in May 2007.

The future. We expect to have product revenues related to our MacroPore Biosurgery segment again when commercialization of the Thin Film products in Japan occurs and we begin Thin Film shipments to Senko.

We also expect to generate product revenues during 2008 related to our regnerative cell therapy segment from the sale of our Celution™ devices and single-use consumables related to breast reconstructive surgery as well as from our newly formed commercialization agreement with Green Hospital Supply, Inc. for regenerative cell banking in Japan signed in August 2007. Refer to Part II, Item 5 for further information.

Cost of product revenues

Cost of product revenues relates to spine and orthopedic products in our MacroPore Biosurgery segment and includes material, manufacturing labor, overhead costs, and an inventory provision, if applicable. The following table summarizes the components of our cost of revenues for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Cost of product revenues	$188,000	$412,000	$ (224,000)	(54.4)%	$403,000	$840,000	$ (437,000)	(52.0)%
Inventory provision	—	70,000	(70,000)	—	—	70,000	(70,000)	—
Share-based compensation	9,000	22,000	(13,000)	(59.1)%	19,000	48,000	(29,000)	(60.4)%
Total cost of product revenues	$197,000	$504,000	$ (307,000)	(60.9)%	$422,000	$958,000	$ (536,000)	(55.9)%
Total cost of product revenues as % of product revenues	38.5%	111.3%			53.3%	100.3%		

MacroPore Biosurgery:

- The decrease in cost of product revenues for the three and six months ended June 30, 2007 as compared to the same periods in 2006 was due largely to a decrease in production of MacroPore Biosurgery spine and orthopedic products, in part due to our sale of the product line in May 2007.

- Cost of product revenues includes approximately $9,000 and $19,000 of share-based compensation expense for the three and six months ended June 30, 2007, respectively. Share-based compensation expense for the three and six months ended June 30, 2006 was $22,000 and $48,000, respectively. For further details, see share-based compensation discussion below.

- During the second quarter of 2006, we recorded a provision of $70,000 related to excess inventory. No such provision was recorded in the first or second quarters of 2007.

The future. We do not expect to incur costs related to our products until commercialization is achieved for our Japan Thin Film product line or until we begin to manufacture the Celution™ device for sale.

Development revenues

The following table summarizes the components of our development revenues for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Regenerative cell technology:								
Development (Olympus)	$1,796,000	$ —	$ 1,796,000	—	$1,796,000	$683,000	$ 1,113,000	163.0%
Research grant (NIH)	—	3,000	(3,000)	—	—	7,000	(7,000)	—
Regenerative cell storage services and other	8,000	54,000	(46,000)	(85.2)%	53,000	56,000	(3,000)	(5.4)%
Total regenerative cell technology	1,804,000	57,000	1,747,000	3,064.9%	1,849,000	746,000	1,103,000	147.9%
MacroPore Biosurgery:								
Development (Senko)	10,000	6,000	4,000	66.7%	10,000	148,000	(138,000)	(93.2)%
Total development revenues	$1,814,000	$63,000	$ 1,751,000	2,779.4%	$1,859,000	$894,000	$ 965,000	107.9%

Regenerative cell technology:

- We recognize deferred revenues, related party, as development revenue when certain performance obligations are met (i.e., using a proportional performance approach). During the three and six months ended June 30, 2007, we recognized $1,796,000 of revenue associated with our arrangements with Olympus. The revenue recognized in the second quarter of 2007 was a result of completion of a preclinical study. During the three and six months ended June 30, 2006, we recognized $0 and $683,000, respectively, of revenue associated with our arrangements with Olympus. The revenue recognized in the first quarter of 2006 was a result of completion of a pre-clinical study and a milestone payment upon receipt of a CE Mark for the first generation Celution™ System.

- The research grant revenue related to a now-completed agreement with NIH. Under this arrangement, the NIH reimbursed us for "qualifying expenditures" related to research on Adipose-Derived Cell Therapy for Myocardial Infarction. Our policy is to recognize revenues under the NIH grant arrangement as the lesser of (i) qualifying costs incurred (and not previously recognized), plus our allowable grant fees for which we are entitled to funding or (ii) the amount determined by comparing the outputs generated to date versus the total outputs expected to be achieved under the research arrangement.

  During the three and six months ended June 30, 2006, we incurred $17,000 and $86,000 in expenditures, of which $3,000 and $7,000 were qualified. We recorded a total of $3,000 and $7,000 in revenues for the three and six months ended June 30, 2006, respectively, which include allowable grant fees as well as cost reimbursements. Our work under this NIH agreement was completed in 2006; as a result, there were no comparable revenues or costs in 2007.

MacroPore Biosurgery:

Under a Distribution Agreement with Senko we are entitled to earn payments based on achieving the following defined milestones:

- Upon notifying Senko of completion of the initial regulatory application to the MHLW for the Thin Film product, we were entitled to a nonrefundable payment of $1,250,000. We so notified Senko on September 28, 2004, received payment in October 2004, and recorded deferred revenues of $1,250,000. As of June 30, 2007, of the amount deferred, we have recognized development revenues of $371,000 ($10,000 in 2007, $152,000 in 2006, $51,000 in 2005, and $158,000 in 2004).

- Under this agreement, we also received a $1,500,000 license fee that was recorded as a component of deferred revenues in the accompanying balance sheet. We are also entitled to a nonrefundable payment of $250,000 once we achieve commercialization. Because the $1,500,000 in license fees is potentially refundable, such amounts will not be recognized as revenues until the refund rights expire. Specifically, half of the license fee is refundable if the parties agree commercialization is not achievable and a proportional amount is refundable if we terminate the arrangement, other than for material breach by Senko, before three years post-commercialization.

The future. We expect to recognize revenues from our regenerative cell technology segment during 2007 as we complete certain pre-clinical studies and certain phases of our product development performance obligations. If we are successful in achieving certain milestone points related to these activities, we will recognize approximately $2,749,000 in revenues during the remainder of 2007. The exact timing of when amounts will be reported in revenue will depend on internal factors (for instance, our ability to complete the service obligations we have agreed to perform) as well as external considerations, including obtaining the necessary regulatory approvals for various therapeutic applications related to the Celution™ System. The cash for these performance obligations was received when the agreement was signed and no further related cash payments will be made to us.

We will continue to recognize revenue from the development work we are performing on behalf of Senko, based on the relative fair value of the milestones completed as compared to the total efforts expected to be necessary to obtain regulatory clearance from the MHLW. We are still

awaiting regulatory clearance from the MHLW in order for initial commercialization to occur. Accordingly, we may recognize approximately $1,129,000 (consisting of $879,000 in deferred revenues plus a non-refundable payment of $250,000 to be received upon commercialization) in revenues associated with this milestone arrangement in 2007, if achieved. Moreover, we expect to recognize $500,000 per year associated with deferred Senko license fees over a three-year period following commercialization as the refund rights associated with the license payment expire.

Research and development expenses

Research and development expenses include costs associated with the design, development, testing and enhancement of our products, regulatory fees, the purchase of laboratory supplies, pre-clinical studies and clinical studies. The following table summarizes the components of our research and development expenses for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Regenerative cell technology:								
Regenerative cell technology	$2,837,000	$3,914,000	$(1,077,000)	(27.5)%	$6,073,000	$ 6,980,000	$ (907,000)	(13.0)%
Development milestone (Joint Venture)	1,329,000	1,513,000	(184,000)	(12.2)%	2,834,000	2,866,000	(32,000)	(1.1)%
Research grants (NIH)	—	17,000	(17,000)	—	—	86,000	(86,000)	—
Share-based compensation	175,000	261,000	(86,000)	(33.0)%	327,000	541,000	(214,000)	(39.6)%
Total regenerative cell technology	4,341,000	5,705,000	(1,364,000)	(23.9)%	9,234,000	10,473,000	(1,239,000)	(11.8)%
MacroPore Biosurgery:								
Bioresorbable polymer implants	30,000	271,000	(241,000)	(88.9)%	111,000	588,000	(477,000)	(81.1)%
Development milestone (Senko)	21,000	37,000	(16,000)	(43.2)%	43,000	115,000	(72,000)	(62.6)%
Share-based compensation	1,000	8,000	(7,000)	(87.5)%	2,000	21,000	(19,000)	(90.5)%
Total MacroPore Biosurgery	52,000	316,000	(264,000)	(83.5)%	156,000	724,000	(568,000)	(78.5)%
Total research and development expenses	$4,393,000	$6,021,000	$(1,628,000)	(27.0)%	$9,390,000	$11,197,000	$(1,807,000)	(16.1)%

Regenerative cell technology:

- Regenerative cell technology expenses relate to the development of a technology platform that involves using adipose tissue as a source for autologous regenerative cells for therapeutic applications. These expenses, in conjunction with our continued development efforts related to our Celution™ System, result primarily from the broad expansion of our research and development efforts enabled by the funding we received from Olympus in 2005 and 2006 and from other investors in 2006 and 2007. Labor-related expenses, not including share-based compensation, decreased by $230,000 for the six months ended June 30, 2007 as compared to the same period in 2006. Professional services expense, which includes pre-clinical study costs, decreased by $1,152,000 for the six months ended June 30, 2007 as compared to the same period in 2006. This was due to decreases in temporary labor, the use of consultants, and a change in focus from pre-clinical studies to clinical studies. Clinical study costs increased by $300,000 for the six months ended June 30, 2007 as compared to the same period in 2006. Rent and utilities expense decreased by $159,000 in the six months ended June 30, 2007 as compared to 2006 due to the new lease terms at our Top Gun location in San Diego, CA. Other supplies decreased by $108,000 during the six months ended June 30, 2007 as compared to 2006. Repairs and maintenance increased by $195,000 for the six months ended June 30, 2007, as compared to the same period in 2006.

- Expenditures related to the Joint Venture with Olympus, which are included in the variation analysis above, include costs that are necessary to support the commercialization of future generation devices based on our Celution™ System. These development activities, which began in November 2005, include performing pre-clinical and clinical studies, seeking regulatory approval, and performing product development related to therapeutic applications for adipose regenerative cells for multiple large markets. For the six months ended June 30, 2007 and 2006, costs associated with the development of the device were $2,834,000 and $2,866,000, respectively. These expenses were composed of $1,719,000 and $1,505,000 in labor and related benefits, $530,000 and $739,000 in consulting and other professional services, $341,000 and $439,000 in supplies and $244,000 and $183,000, respectively, in other miscellaneous expense.

- In 2004, we entered into an agreement with the NIH to reimburse us for up to $950,000 (Phase I $100,000 and Phase II $850,000) in "qualifying expenditures" related to research on Adipose-Derived Cell Therapy for Myocardial Infarction. For the three and six months ended June 30, 2006, we incurred $17,000 and $86,000 of direct expenses relating entirely to Phase II ($14,000 and $79,000 of which were not reimbursed, respectively). Our work under this NIH agreement was completed during 2006; as a result, there were no comparable costs in 2007.

- Share-based compensation for the regenerative cell technology segment of research and development was $175,000 and $327,000 for the three and six months ended June 30, 2007, respectively. Share-based compensation was $262,000 and $541,000 for the three and six months ended June 30, 2006, respectively. See share-based compensation discussion below for more details.

MacroPore Biosurgery:

- Labor and related benefits expense, not including share-based compensation, decreased by $177,000 for the six months ended June 30, 2007 as

compared to the same period in 2006. This was due to a redistribution of labor resources from one business segment to the other, as well as to termination of spine and orthopedics product research upon sale of that product line in May 2007.

- Under a Distribution Agreement with Senko, we are responsible for the completion of the initial regulatory application to the MHLW and commercialization of the Thin Film product line in Japan. Commercialization occurs when one or more Thin Film product registrations are completed with the MHLW. During the three and six months ended June 30, 2007, we incurred $28,000 of expenses related to this regulatory and registration process. We incurred $37,000 and $115,000 of expenses for the same periods in 2006.

- Share-based compensation for the MacroPore Biosurgery segment of research and development for the three and six months ended June 30, 2007 was $1,000 and $2,000, respectively. Share-based compensation was $8,000 and $21,000, respectively, for the three and six months ended June 30, 2006. See share-based compensation discussion below for more details.

The future. Our strategy is to continue to increase our research and development efforts in the regenerative cell field and we anticipate expenditures in this area of research to total approximately $22,000,000 to $24,000,000 in 2007. We are working to develop therapies for cardiovascular disease as well as new approaches for aesthetic and reconstructive surgery, gastrointestinal disorders and spine and orthopedic conditions. We are also developing a regenerative cell banking platform for use in hospitals and clinics that will preserve harvested regenerative cells for potential future use. The expenditures have and will continue to primarily relate to developing therapeutic applications and conducting pre-clinical and clinical studies on adipose-derived regenerative cells.

Sales and marketing expenses

Sales and marketing expenses include costs of marketing personnel, tradeshows, physician training, and promotional activities and materials. Before the sale of our spine and orthopedic implant product line in May 2007, Medtronic was responsible for the distribution, marketing, and sales support of our spine and orthopedic devices. The following table summarizes the components of our sales and marketing expenses for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Regenerative cell technology:								
International sales and marketing	$412,000	$313,000	$ 99,000	31.6%	$ 846,000	$600,000	$ 246,000	41.0%
Share-based compensation	65,000	87,000	(22,000)	(25.3)%	135,000	188,000	(53,000)	(28.2)%
Total regenerative cell technology	477,000	400,000	77,000	19.3%	981,000	788,000	193,000	24.5%
MacroPore Biosurgery:								
General corporate marketing	8,000	47,000	(39,000)	(83.0)%	21,000	130,000	(109,000)	(83.8)%
International sales and marketing	34,000	24,000	10,000	41.7%	63,000	47,000	16,000	34.0%
Share-based compensation	—	2,000	(2,000)	—	—	9,000	(9,000)	—
Total MacroPore Biosurgery	42,000	73,000	(31,000)	(42.5)%	84,000	186,000	(102,000)	(54.8)%
Total sales and marketing expenses	$519,000	$473,000	$ 46,000	9.7%	$1,065,000	$974,000	$ 91,000	9.3%

Regenerative Cell Technology:

- International sales and marketing expenditures for the three and six months ended June 30, 2007 and 2006 relate primarily to salary expenses for employees involved in business development. The main emphasis of these newly-formed functions is to seek strategic alliances and/or co-development partners for our regenerative cell technology.

- Share-based compensation for the regenerative cell segment of sales and marketing for the three and six months ended June 30, 2007 was $65,000 and $135,000, respectively. Share-based compensation for the regenerative cell segment of sales and marketing for the three and six months ended June 30, 2006 was $87,000 and $188,000, respectively. See share-based compensation discussion below for more details.

MacroPore Biosurgery:

- General corporate marketing expenditures relate to expenditures for maintaining our corporate image and reputation within the research and surgical communities relevant to bioresorbable implants. Expenditures in this area continued to decrease as we focused more on our regenerative cell technology business and prepared to exit from our spine and orthopedic implant business.

- International sales and marketing expenditures relate to costs associated with developing an international bioresorbable Thin Film distributor and supporting a bioresorbable Thin Film sales office in Japan.

- Share-based compensation for the MacroPore Biosurgery segment of sales and marketing for the three and six months ended June 30, 2007 was $0. Share-based compensation for the MacroPore Biosurgery segment of sales and marketing for the three and six months ended June 30, 2006 was $2,000 and $9,000, respectively. See share-based compensation discussion below for more details.

The future. We expect sales and marketing expenditures related to the regenerative cell technology to increase as we continue to expand our pursuit of strategic alliances and co-development partners, as well as market our Celution™ System, which is expected to be commercialized in 2008.

General and administrative expenses

General and administrative expenses include costs for administrative personnel, legal and other professional expenses, and general corporate expenses. The following table summarizes the general and administrative expenses for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
General and administrative	$3,076,000	$2,919,000	$ 157,000	5.4%	$5,927,000	$5,758,000	$ 169,000	2.9%
Share-based compensation	357,000	689,000	(332,000)	(48.2)%	672,000	1,066,000	(394,000)	(37.0)%
Total general and administrative expenses	$3,433,000	$3,608,000	$ (175,000)	(4.9)%	$6,599,000	$6,824,000	$ (225,000)	(3.3)%

- Professional services costs increased by $310,000 during the six month ended June 30, 2007 as compared to the same period in 2006 due to the increased use of financial and business advisory services. This was offset by a decrease of $122,000 in depreciation and amortization for the six months ended June 30, 2007, compared to the same period in 2006.

- We have incurred substantial legal expenses in connection with the University of Pittsburgh's 2004 lawsuit. Although we are not litigants and are not responsible for any settlement costs, if the University of Pittsburgh wins the lawsuit our license rights to the patent in question could be nullified or rendered non-exclusive. The amended license agreement signed with the Regents of the University of California ("UC") in the third quarter of 2006 clarified that we are responsible for all patent prosecution and litigation costs related to this lawsuit. In the three and six months ended June 30, 2007, we expensed $518,000 and $602,000, respectively, for legal fees related to this license. For the same periods in 2006, we expensed $861,000 and $1,366,000, respectively. Our legal expenses related to this lawsuit will fluctuate depending upon the activity incurred during each period.

- Share-based compensation related to general and administrative expense for the three and six months ended June 30, 2007 was $357,000 and $672,000, respectively. Share-based compensation related to general and administrative expense for the same periods in 2006 was $689,000 and $1,066,000, respectively. See share-based compensation discussion below for more details.

The future. We expect general and administrative expenses of approximately $11,000,000 in 2007. We will seek ways to minimize the ratio of these expenses to research and development expenses.

We expect to continue to incur substantial legal expenses in connection with the University of Pittsburgh's 2004 lawsuit and for the forseeable future.

Share-based compensation expenses

We adopted SFAS 123R on January 1, 2006. The following table summarizes the components of our share-based compensation for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Regenerative cell technology:								
Research and development-related	$175,000	$ 261,000	$ (86,000)	(33.0)%	$ 327,000	$ 541,000	$ (214,000)	(39.6)%
Sales and marketing-related	65,000	87,000	(22,000)	(25.3)%	135,000	188,000	(53,000)	(28.2)%
Total regenerative cell technology	240,000	348,000	(108,000)	(31.0)%	462,000	729,000	(267,000)	(36.6)%
MacroPore Biosurgery:								
Cost of product revenues	9,000	22,000	(13,000)	(59.1)%	19,000	48,000	(29,000)	(60.4)%
Research and development-related	1,000	8,000	(7,000)	(87.5)%	2,000	21,000	(19,000)	(90.5)%
Sales and marketing-related	—	2,000	(2,000)	—	—	9,000	(9,000)	—
Total MacroPore Biosurgery	10,000	32,000	(22,000)	(68.8)%	21,000	78,000	(57,000)	(73.1)%
General and administrative-related	357,000	689,000	(332,000)	(48.2)%	672,000	1,066,000	(394,000)	(37.0)%

Total share-based compensation	$607,000	$1,069,000	$ (462,000)	(43.2)%	$1,155,000	$1,873,000	$ (718,000)	(38.3)%

During the first quarter of 2007, we issued to our officers and directors stock options to purchase up to 410,000 shares of our common stock, with a four-year vesting for our officers and 24-month vesting for our directors. The grant date fair value of option awards granted to our officers and directors was $3.82 and $3.70 per share, respectively. The resulting share-based compensation expense of $1,480,000, net of estimated forfeitures, will be recognized as expense over the respective vesting periods.

During the second quarter of 2007, we made a company-wide option grant to our non-executive employees to purchase up to 213,778 shares of our common stock, subject to a four-year vesting schedule. The grant date fair value for the awards was $3.66 per share. The resulting share-based compensation expense of $739,000, net of estimated forfeitures, will be recognized as expense over the respective vesting periods.

The future. We will continue to grant options (which will result in an expense) to our employees and, as appropriate, to non-employee service providers. In addition, previously-granted options will continue to vest in accordance with their original terms. As of June 30, 2007, the total compensation cost related to non-vested stock options not yet recognized for all our plans is approximately $5,269,000. These costs are expected to be recognized over a weighted average period of 1.87 years.

Gain on sale of assets

The following is a table summarizing the gain on sale of assets from the disposal of our spine and orthopedic product line for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Gain on sale of assets	$1,858,000	$ —	$ 1,858,000	—	$1,858,000	$ —	$ 1,858,000	—
Total gain on sale of assets	$1,858,000	$ —	$ 1,858,000	—	$1,858,000	$ —	$ 1,858,000	—

- In May 2007, we sold to Kensey Nash our intellectual property rights and tangible assets related to our spine and orthopedic bioresorbable implant product line, a part of our MacroPore Biosurgery business. Excluded from the sale was our Japan Thin Film product line. We received $3,175,000 in cash related to the disposition. The assets comprising the spine and orthopedic product line transferred to Kensey Nash were as follows:

	Carrying Value Prior to Disposition
Inventory	$ 94,000
Other current assets	17,000
Assets held for sale	436,000
Goodwill	465,000
	$ 1,012,000

- We incurred expenses of $109,000 in connection with the sale. We recognized approximately $1,858,000 as gain on sale in the statement of operations during the second quarter of 2007. The revenues and expenses related to the spine and orthopedic product line transferred to Kensey Nash for the three and six months ended June 30, 2007 and 2006 were as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2007	2006	2007	2006
Revenues	$ 512,000	$ 453,000	$ 792,000	$ 955,000
Cost of product revenues	(197,000)	(504,000)	(422,000)	(958,000)
Research & development	(31,000)	(279,000)	(113,000)	(609,000)
Sales & marketing	(8,000)	(50,000)	(21,000)	(138,000)

- As part of the disposition agreement, we are required to provide training to Kensey Nash representatives in all aspects of the manufacturing process related to the transferred spine and orthopedic product line, and to act in the capacity of a product manufacturer from the point of sale through August 2007. Because of these additional manufacturing requirements, we deferred $196,000 of the gain related to the outstanding manufacturing requirements to be completed by August 31, 2007.

Change in fair value of option liabilities

The following is a table summarizing the change in fair value of option liabilities for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Change in fair value of option liability	$ —	$(2,765,000)	$ 2,765,000	—	$ —	$(3,140,000)	$ 3,140,000	—
Change in fair value of put option liability	(100,000)	100,000	(200,000)	(200.0)%	100,000	—	100,000	—
Total change in fair value of option liabilities	$(100,000)	$(2,665,000)	$ 2,565,000	(96.2)%	$100,000	$(3,140,000)	$ 3,240,000	(103.2)%

- We granted Olympus an option to acquire 2,200,000 shares of our common stock which expired December 31, 2006. The exercise price of the option shares was $10 per share. We had accounted for this grant as a liability because had the option been exercised, we would have been required to deliver listed shares of our common stock to settle the option shares. In accordance with EITF 00-19, the fair value of this option was re-measured at the end of each quarter, using the Black-Scholes option pricing model, with the movement in fair value reported in the statement of operations as a change in fair value of option liabilities.

- In reference to the Joint Venture, the Shareholders' Agreement between Cytori and Olympus provides that in certain specified circumstances of insolvency or if we experience a change in control, Olympus will have the rights to (i) repurchase our interests in the Joint Venture at the fair value of such interests or (ii) sell its own interests in the Joint Venture to us at the higher of (a) $22,000,000 or (b) the Put's fair value. The Put value has been classified as a liability.

  The valuations of the Put were completed by an independent valuation firm using an option pricing theory-based simulation analysis (i.e., a Monte Carlo simulation). The valuations are based on assumptions as of the valuation date with regard to the market value of Cytori and the estimated fair value of the Joint Venture, the expected correlation between the values of Cytori and the Joint Venture, the expected volatility of Cytori and the Joint Venture, the bankruptcy recovery rate for Cytori, the bankruptcy threshold for Cytori, the probability of a change of control event for Cytori, and the risk-free interest rate.

  The following assumptions were employed in estimating the value of the Put:

	June 30, 2007	December 31, 2006	November 4, 2005
Expected volatility of Cytori	61.00%	66.00%	63.20%
Expected volatility of the Joint Venture	61.00%	56.60%	69.10%
Bankruptcy recovery rate for Cytori	21.00%	21.00%	21.00%
Bankruptcy threshold for Cytori	$ 10,460,000	$ 10,110,000	$ 10,780,000
Probability of a change of control event for Cytori	2.22%	1.94%	3.04%
Expected correlation between fair values of Cytori and the Joint Venture in the future	99.00%	99.00%	99.00%
Risk-free interest rate	5.03%	4.71%	4.66%

The future. The Put has no expiration date. Accordingly, we will continue to recognize a liability for the Put until it is exercised or until the arrangements with Olympus are amended.

Income taxes

On July 13, 2006, the FASB issued FIN 48, which clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS 109, and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Under FIN 48, the impact of an uncertain income tax position on the income tax return must be recognized at the largest amount that is more-likely-than-not to be sustained upon audit by the relevant taxing authority. An uncertain income tax position will not be recognized if it has less than a 50% likelihood of being sustained. Additionally, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006.

We adopted the provisions of FIN 48 on January 1, 2007. There were no unrecognized tax benefits as of the date of adoption. There are no unrecognized tax benefits included in the balance sheet that would, if recognized, affect the effective tax rate.

Our practice is to recognize interest and/or penalties related to income tax matters in income tax expense. We had $0 accrued for interest and penalties on our balance sheet as of June 30, 2007 and December 31, 2006, and have recognized $0 in interest and/or penalties in our statement of operations for the three and six months ended June 30, 2007.

With limited exception, we are subject to taxation in the U.S. and California jurisdictions. Our tax years for 1997 and forward are subject to examination by the U.S. and California tax authorities due to the carryforward of unutilized net operating losses and research and development credits.

The adoption of FIN No. 48 did not impact our financial condition, results of operations or cash flows. At January 1, 2007, we had net deferred tax assets of $38,505,000 million. The deferred tax assets are primarily composed of federal and state tax net operating loss carryforwards and federal and state R&D credit carryforwards. Due to uncertainties surrounding our ability to generate future taxable income to realize these assets, a full valuation allowance has been established to offset our deferred tax asset. Additionally, the future utilization of our net operating loss and R&D credit carryforwards to offset future taxable income may be subject to a substantial annual limitation as a result of ownership changes that may have occurred previously or that could occur in the future. We are in the process of updating our Section 382/383 analysis through the period ending December 31, 2006. We have not yet determined whether such an ownership change has occurred, however, the Company is currently working to complete a Section 382/383 analysis regarding the limitation of the net operating losses and research and development credits. Similarly, we plan to complete an R&D credit analysis regarding the calculation of the R&D credit. When these analyses are completed, we may need to update the amount of unrecognized tax benefits we have reported under FIN No. 48. Therefore, we expect that the unrecognized tax benefits may change within 12 months of this reporting date. At this time, we cannot estimate how much the unrecognized tax benefits may change. Due to the existence of the valuation allowance, future changes in our unrecognized tax benefits will not impact our effective tax rate.

Financing items

The following table summarizes interest income, interest expense, and other income and expense for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Interest income	$348,000	$183,000	$ 165,000	90.2%	$545,000	$ 379,000	$ 166,000	43.8%
Interest expense	(43,000)	(53,000)	10,000	(18.9)%	(95,000)	(111,000)	16,000	(14.4)%
Other income (expense)	(52,000)	(1,000)	(51,000)	5,100.0%	(54,000)	(6,000)	(48,000)	800.0%
Total	$253,000	$129,000	$ 124,000	96.1%	$396,000	$ 262,000	$ 134,000	51.1%

- Interest income increased for the three and six months ended June 30, 2007 due to an increased cash balance available for investment.
- Interest expense decreased in 2007 as compared to 2006 due to lower principal balances on our long-term equipment-financed borrowings offset by an additional promissory note of approximately $600,000 executed in December 2006.
- The changes in other income (expense) in the first quarter of 2007 as compared to the same period in 2006 resulted primarily from changes in foreign currency exchange rates.

The future. Interest income earned in 2007 will be dependent on our levels of funds available for investment as well as general economic conditions. We expect interest expense to remain relatively consistent during the remainder of 2007.

Equity gain (loss) from investment in Joint Venture

The following table summarizes our equity loss from investment in joint venture for the three and six months ended June 30, 2007 and 2006:

	For the three months ended June 30,				For the six months ended June 30,			
	2007	2006	$ Differences	% Differences	2007	2006	$ Differences	% Differences
Equity gain (loss) in	$9,000	$(17,000)	$ 26,000	(152.9)%	$6,000	$(66,000)	$ 72,000	(109.1)%

investment								

The losses in 2006 relate entirely to our 50% equity interest in the Joint Venture, which we account for using the equity method of accounting. We experienced a small gain with relation to this investment during the three and six months ended June 30, 2007. This was due to an adjustment to an estimated expense.

The future. We do not expect to recognize significant losses from the activities of the Joint Venture in the foreseeable future. Over the next two to three years, the Joint Venture is expected to incur general and administrative expenses. Though we have no obligation to do so, we and Olympus plan to jointly fund the Joint Venture to cover any costs should the Joint Venture deplete its cash balance.

Liquidity and Capital Resources

Short-term and long-term liquidity

The following is a summary of our key liquidity measures at June 30, 2007 and December 31, 2006:

	June 30, 2007	December 31, 2006	$ Differences	% Differences
Cash and cash equivalents	$ 22,808,000	$ 8,902,000	$ 13,906,000	156.2%
Short-term investments, available for sale	3,795,000	3,976,000	(181,000)	(4.6)%
Total cash and cash equivalents and short-term investments, available for sale	$ 26,603,000	$ 12,878,000	13,725,000	106.6%
Current assets	$ 27,304,000	$ 13,978,000	$ 13,326,000	95.3%
Current liabilities	5,598,000	6,586,000	(988,000)	(15.0)%
Working capital	$ 21,706,000	$ 7,392,000	$ 14,314,000	193.6%

In order to provide greater financial flexibility and liquidity, and in view of the substantial cash needs of our regenerative cell business, we have an ongoing need to raise additional capital. In the third quarter of 2006, we received net proceeds of $16,219,000 from the sale of common stock pursuant to a shelf registration statement, of which Olympus purchased $11,000,000; the remaining shares were purchased by other institutional investors. Additionally, in the first quarter of 2007, we received net proceeds of $19,901,000 from the sale of units consisting of 3,746,000 shares of common stock and 1,873,000 common stock warrants (with an exercise price of $6.25 per share) under the shelf registration statement. In the second quarter of 2007, we received net proceeds of $6,000,000 from the sale of 1,000,000 shares of common stock to Green Hospital Supply, Inc. in a private placement. Also in the second quarter of 2007, we successfully divested our spine and orthopedic product line to Kensey Nash for gross proceeds of $3,175,000.

With consideration of these endeavors as well as existing funds, cash generated by operations, and other accessible sources of financing, we believe our cash position is adequate to satisfy our working capital, capital expenditures, debt service, and other financial commitments at least through June 30, 2008.

From inception to June 30, 2007, we have financed our operations primarily by:

- Issuing our stock in pre-IPO transactions, in our 2000 initial public offering in Germany, and upon stock option exercises,
- Generating revenues,
- Selling the bioresorbable implant CMF product line in September 2002,
- Selling the bioresorbable implant Thin Film product line (except for the territory of Japan), in May 2004,
- Entering into a Distribution Agreement for the distribution rights to Thin Film in Japan, in which we received an upfront license fee in July 2004 and an initial development milestone payment in October 2004,
- Obtaining a modest amount of capital equipment long-term financing,
- Issuing 1,100,000 shares of common stock to Olympus under a Stock Purchase Agreement which closed in May 2005,
- Entering into a collaborative arrangement with Olympus in November 2005, including the formation of a joint venture called Olympus-Cytori, Inc.,
- Receiving funds in exchange for granting Olympus an exclusive right to negotiate in February 2006,
- Receiving net proceeds of $16,219,000 from the sale of common stock under our shelf registration statement in August 2006,
- Receiving net proceeds of $19,901,000 from the sale of common stock and common stock warrants under the shelf registration statement in February 2007.
- Receiving net proceeds of $6,000,000 from the common stock private placement to Green Hospital Supply, Inc., in April 2007.
- Receiving gross proceeds of $3,175,000 from the sale of our spine and orthopedic product line to Kensey Nash in May 2007.

We don’t expect significant capital expenditures during the remainder of 2007; however, if necessary, we may borrow under our Amended Master Security Agreement.

Any excess funds will be invested in short-term available-for-sale investments.

Our cash requirements for 2007 and beyond will depend on numerous factors, including the resources we devote to developing and supporting our investigational cell therapy products, market acceptance of any developed products, regulatory approvals, and other factors. We expect to incur research and development expenses at high levels in our regenerative cell platform for an extended period of time and have therefore positioned ourselves to expand our

cash position through actively pursuing co-development and marketing agreements, research grants, and licensing agreements related to our regenerative cell technology platform.

The following summarizes our contractual obligations and other commitments at June 30, 2007, and the effect such obligations could have on our liquidity and cash flow in future periods:

	Payments due by period				
Contractual Obligations	**Total**	**Less than 1 year**	**1 - 3 years**	**3 - 5 years**	**More than 5 years**
Long-term obligations	$ 1,384,000	$ 771,000	$ 613,000	$ —	$ —
Interest commitment on long-term obligations	147,000	108,000	39,000	—	—
Operating lease obligations	4,233,000	1,468,000	2,765,000	—	—
Pre-clinical research study obligations	267,000	267,000	—	—	—
Clinical research study obligations	6,314,000	5,458,000	856,000	—	—
Total	$12,345,000	$ 8,072,000	$ 4,273,000	$ —	$ —

Cash (used in) provided by operating, investing, and financing activities for the six months ended June 30, 2007 and 2006 is summarized as follows:

	For the six months ended June 30,	
	2007	**2006**
Net cash used in operating activities	$ (15,009,000)	$ (4,188,000)
Net cash provided by (used in) investing activities	2,880,000	(1,631,000)
Net cash provided by financing activities	26,035,000	191,000

Operating activities

Net cash (used in) provided by operating activities for both periods presented resulted primarily from expenditures related to our regenerative cell research and development efforts.

Research and development efforts, other operational activities, and a comparatively small amount of product sales generated a $12,665,000 net loss for the six months ended June 30, 2007. The operating cash impact of this loss was $15,009,000, after adjusting for the gain on sale of our spine and orthopedic product line (considered an investing activity), the recognition of non-cash development revenue, share-based compensation of $1,155,000, other adjustments including material non-cash activities, such as depreciation and amortization, and changes in working capital due to timing of product shipments (accounts receivable) and payment of liabilities.

Research and development efforts, other operational activities, and a comparatively small amount of product sales generated a $14,768,000 net loss for the six months ended June 30, 2006. The cash impact of this loss was $4,188,000, after adjusting for the $11,817,000 we received from Olympus in the first half of the year. Other adjustments include material non-cash activities, such as depreciation and amortization, changes in the fair value of the Olympus option liabilities, share-based compensation expense, and equity loss from investment in Joint Venture, as well as changes in working capital due to the timing of product shipments (accounts receivable) and payment of liabilities.

Investing activities

Net cash provided by investing activities for the six months ended June 30, 2007 resulted primarily from proceeds from the sale of our spine and orthopedics bioresorbable implant product line to Kensey Nash.

Net cash used in investing activities for the six months ended June 30, 2006 resulted primarily from expenditures for leasehold improvements, offset in part by the net proceeds from the sale of short-term investments.

Capital spending is essential to our product innovation initiatives and to maintain our operational capabilities. For the six months ended June 30, 2007 and 2006, we used cash to purchase $365,000 and $2,331,000, respectively, of property and equipment, primarily, to support the research and development of the regenerative cell technology platform. The high level of 2006 capital spending was caused primarily by expenditures for leasehold improvements made to our new Callan Road facilities.

Financing Activities

The net cash provided by financing activities for the six months ended June 30, 2007 related mainly to the issuance of 3,746,000 shares of our common stock and 1,873,000 common stock warrants in exchange for approximately $21,500,000 ($19,901,000 net of direct offering costs) as well as the sale of 1,000,000 shares of treasury stock for $6,000,000.

The net cash provided by financing activities for the year ended June 30, 2006 related mainly to the exercise of employee stock options offset by the principal payments on long-term obligations.

Critical Accounting Policies and Significant Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of our assets, liabilities, revenues, and expenses, and that affects our recognition and disclosure of

contingent assets and liabilities.

While our estimates are based on assumptions we consider reasonable at the time they were made, our actual results may differ from our estimates, perhaps significantly. If results differ materially from our estimates, we will make adjustments to our financial statements prospectively as we become aware of the necessity for an adjustment.

We believe it is important for you to understand our most critical accounting policies. These are policies that require us to make our most significant judgments and, as a result, could have the greatest impact on our future financial results.

Revenue Recognition

We derive our revenue from a number of different sources, including but not limited to:

- Fees for achieving certain defined milestones under research and/or development arrangements,
- Product sales, and
- Payments under license or distribution agreements.

A number of our revenue-generating arrangements are relatively simple in nature, meaning that there is little judgment necessary with regard to the timing of when we recognize revenues or how such revenues are presented in the financial statements.

However, we have also entered into more complex arrangements, including but not limited to our contracts with Olympus and Senko. Moreover, some of our non-recurring transactions, such as our disposition of the majority of our Thin Film business to MAST, contain elements that relate to our product revenue-producing activities.

As a result, some of our most critical accounting judgments relate to the identification, timing, and presentation of revenue-related activities. These critical judgments are discussed further in the paragraphs that follow.

Multiple-elements

Some of our revenue-generating arrangements contain a number of distinct revenue streams, known as “elements.” For example, our Distribution Agreement with Senko contains direct or indirect future revenue streams related to:

- A distribution license fee (which was paid at the outset of the arrangement),
- Milestone payments for achieving commercialization of the Thin Film product line in Japan,
- Training for representatives of Senko,
- Sales of Thin Film products to Senko, and
- Payments in the nature of royalties on future product sales made by Senko to its end customers.

EITF 00-21 governs whether each of the above elements in the arrangement should be accounted for individually, or whether the entire contract should be treated as a single unit of accounting.

EITF 00-21 indicates that individual elements may be separately accounted for only when:

- The delivered element has stand-alone value to the customer,
- There is objective evidence of the fair value of the remaining undelivered elements, and
- If the arrangement contains a general right of return related to any products delivered, and delivery of the remaining goods and services is probable and within the complete control of the seller.

In the case of the Senko Distribution Agreement, we determined that (a) the milestone payments for achieving commercialization and (b) the future sale of Thin Film products to Senko were “separable” elements. That is, each of these elements, upon delivery, will have stand-alone value to Senko and there will be objective evidence of the fair value of any remaining undelivered elements at that time. The arrangement does not contain any general right of return, and so this point is not relevant to our analysis.

On the other hand, we concluded that (a) the upfront distribution license fee, (b) the revenues from training for representatives of Senko, and (c) the payments in the form of royalties on future product sales are not separable elements under EITF 00-21.

In arriving at our conclusions, we had to consider whether our customer, Senko, would receive stand-alone value from each delivered element. We also, in some cases, had to look to third-party evidence to support the fair value of certain undelivered elements - notably, training - since we as a company do not routinely deliver this service on a stand-alone basis. Finally, we had to make assumptions about how the non-separable elements of the arrangement are earned, particularly the estimated period over which Senko will benefit from the arrangement (refer to the "Recognition" discussion below for further background).

We also agreed to perform multiple services under the November 4, 2005 agreements we signed with Olympus, including:

- Granting the Joint Venture (which Olympus is considered to control) an exclusive and perpetual manufacturing license to our device technology, including the Celution™ System and certain related intellectual property; and

- Performing development activities in relation to certain therapeutic applications associated with our Celution™ System, including completing pre-clinical and clinical trials, seeking regulatory approval as appropriate, and assisting with product development.

We concluded that the license and development services must be accounted for as a single unit of accounting. In reaching this conclusion, we determined that the license would not have stand-alone value to the Joint Venture. This is because Cytori is the only party that could be reasonably expected to perform the development services, including pre-clinical and clinical studies, regulatory filings, and product development assistance, necessary for the Joint Venture to derive any value from the license.

Recognition

Besides determining whether to account separately for components of a multiple-element arrangement, we also use judgment in determining the appropriate accounting period in which to recognize revenues that we believe (a) have been earned and (b) are realizable. The following describes the recognition issue with regard to upfront license fees and milestones that we have considered during the reporting period:

- As part of the Senko Distribution Agreement, we received an upfront license fee upon execution of the arrangement, which, as noted previously, was not separable under EITF 00-21. Accordingly, the license has been combined with the development (milestones) element, which was separable, to form a single accounting unit. This single element of $3,000,000 in fees includes $1,500,000 which is potentially refundable. We have recognized, and will continue to recognize, the non-contingent fees allocated to this combined element as revenues as we complete each of the performance obligations associated with the milestones component of this combined deliverable. Note that the timing of when we have recognized revenues to date does not correspond with the cash we received upon achieving certain milestones. For example, the first such milestone payment for $1,250,000 became payable to us when we filed a commercialization application with the Japanese regulatory authorities. However, we determined that the payment received was not commensurate with the level of effort expended, particularly when compared with other steps we believe are necessary to commercialize the Thin Film product line in Japan. Accordingly, we did not recognize the entire $1,250,000 received as revenues, but instead initially classified this amount as deferred revenues. Approximately $371,000 ($10,000 in 2007, $152,000 in 2006, $51,000 in 2005, and $158,000 in 2004) has been recognized to date as development revenues based on our estimates of the level of effort expended for completed milestones as compared with the total level of effort we expect to incur under the arrangement to successfully achieve regulatory approval of the Thin Film product line in Japan. These estimates were subject to judgment and there may be changes in estimates regarding the total level of effort as we continue to seek regulatory approval. In fact, there can be no assurance that commercialization in Japan will ever be achieved, as we have yet to receive definitive notification from the MHLW.

- We also received upfront fees as part of the Olympus arrangements (although, unlike in the Senko agreement, these fees were non-refundable). Specifically, in exchange for an upfront fee, we granted the Joint Venture an exclusive, perpetual license to certain of our intellectual property and agreed to perform additional development activities. This upfront fee has been recorded in the liability account entitled deferred revenues, related party, on our consolidated balance sheet. Similar to the Senko agreement, we have elected an accounting policy to recognize revenues from the combined license/development accounting unit as we perform the development services, as this represents our final obligation underlying the combined accounting unit. Specifically, we have recognized revenues from the license/development accounting unit using a "proportional performance" methodology, resulting in the derecognition of amounts recorded in the deferred revenues, related party account as we complete various milestones underlying the development services. For instance, we have recognized and will continue to recognize some of the deferred revenues, related party, as revenues, related party, when we complete a pre-clinical trial or obtain regulatory approval in a specific jurisdiction. Determining what portion of the deferred revenues, related party balance to recognize as each milestone is completed involves substantial judgment. In allocating the balance of the deferred revenues, related party, to various milestones, we had in-depth discussions with our operations personnel regarding the relative value of each milestone to the Joint Venture and Olympus. We also considered the cost of completing each milestone relative to the total costs we plan to incur in completing all of the development activities, since we believe that the relative cost of completing a milestone is a reasonable proxy for its fair value. The accounting policy described above could result in revenues being recorded in an earlier accounting period than had other judgments or assumptions been made by us.

Goodwill Impairment Testing

In late 2002, we purchased StemSource, Inc. and recognized over $4,600,000 in goodwill associated with the acquisition, of which $3,922,000 remains on our balance sheet as of June 30, 2007. As required by Statement of Financial Accounting Standard No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"), we must test this goodwill at least annually for impairment as well as when an event occurs or circumstances change such that it is reasonably possible that impairment may exist. Moreover, this testing must be performed at a level of the organization known as the reporting unit. A reporting unit is at least the same level as a company's operating segments, and sometimes even one level lower. Our two reporting units are, in fact, our two operating segments.

Specifically, the process for testing goodwill for impairment under SFAS 142 involves the following steps:

- Company assets and liabilities, including goodwill, are allocated to each reporting unit for purposes of completing the goodwill impairment test.
- The carrying value of each reporting unit - that is, the sum of all of the net assets allocated to the reporting unit - is then compared to its fair value.
- If the fair value of the reporting unit is lower than its carrying amount, goodwill may be impaired - additional testing is required.

When we last completed our goodwill impairment testing in 2006, the fair values of our two reporting units each exceeded their respective carrying values. Accordingly, we determined that none of our reported goodwill was impaired.

The application of the goodwill impairment test involves a substantial amount of judgment. For instance, SFAS 142 requires that assets and liabilities be assigned to a reporting unit if both of the following criteria are met:

- The asset will be employed in or the liability relates to the operations of a reporting unit.
- The asset or liability will be considered in determining the fair value of the reporting unit.

We developed mechanisms to assign company-wide assets like shared property and equipment, as well as company-wide obligations such as borrowings under our GE loan facility, to our two reporting units. In some cases, certain assets were not allocable to either reporting unit and were left unassigned.

The most complex and challenging asset to assign to each reporting unit was our acquired goodwill. As noted previously, all of our recorded goodwill was generated in connection with our acquisition of StemSource in 2002. However, when we first acquired StemSource, we determined that a portion of the goodwill related to the MacroPore Biosurgery reporting unit. The amount of goodwill allocated represented our best estimate of the synergies (notably future cost savings from shared research and development activities) that the MacroPore Biosurgery reporting unit would obtain by virtue of the acquisition.

Finally, with the consultation and assistance of a third party, we estimated the fair value of our reporting units by using various estimation techniques.

- In particular, in 2006, we estimated the fair value of our MacroPore Biosurgery reporting unit based on an equal weighting of the market values of comparable enterprises and discounted projections of estimated future cash flows. Clearly, identifying comparable companies and estimating future cash flows as well as appropriate discount rates involve judgment. The $465,000 of goodwill determined to be related to our MacroPore Biosurgery reporting unit was transferred to Kensey Nash upon the sale of our spine and orthopedic product line in 2007. Therefore, as of June 30, 2007, all of our goodwill relates to our regenerative cell business.
- On the contrary, we estimated the fair value of our regenerative cell reporting unit solely using an income approach, as we believe there are no comparable enterprises on which to base a valuation. The assumptions underlying this valuation method involve a substantial amount of judgment, particularly since our regenerative cell business has yet to generate any revenues and does not have a commercially viable product. The combined value of our goodwill is consistent with the market's valuation.

Again, the manner in which we assigned assets, liabilities, and goodwill to our reporting units, as well as how we determined the fair value of such reporting units, involves significant uncertainties and estimates. The judgments employed may have an effect on whether a goodwill impairment loss is recognized.

Variable Interest Entity (Olympus-Cytori Joint Venture)

FASB Interpretation No. 46 (revised 2003), "Consolidation of Variable Interest Entities - an Interpretation of ARB No. 51" ("FIN 46R") requires a variable interest entity ("VIE") to be consolidated by its primary beneficiary. Evaluating whether an entity is a VIE and determining its primary beneficiary involves significant judgment.

In concluding that the Olympus-Cytori Joint Venture was a VIE, we considered the following factors:

- Under FIN 46R, an entity is a VIE if it has insufficient equity to finance its activities. We recognized that the initial cash contributed to the Joint Venture formed by Olympus and Cytori ($30,000,000) would be completely utilized by the first quarter of 2006. Moreover, it was highly unlikely that the Joint Venture would be able to obtain the necessary financing from third-party lenders without additional subordinated financial support - such as personal guarantees by one or both of the Joint Venture stockholders. Accordingly, the Joint Venture will require additional financial support from Olympus and Cytori to finance its ongoing operations, indicating that the Joint Venture is a VIE. In fact, in the first quarter of 2006, we contributed $150,000 each to fund the Joint Venture's ongoing operations.

- Moreover, Olympus has a contingent put option that would, in specified circumstances, require Cytori to purchase Olympus's interests in the Joint Venture for a fixed amount of $22,000,000. Accordingly, Olympus is protected in some circumstances from absorbing all expected losses in the Joint Venture. Under FIN 46R, this means that Olympus may not be an "at-risk" equity holder, although Olympus clearly has decision rights over the operations of the Joint Venture.

Because the Joint Venture is undercapitalized, and because one of the Joint Venture's decision makers may be protected from losses, we have determined that the Joint Venture is a VIE under FIN 46R. Because of the complexities in applying FIN 46R, it is reasonable to expect that others may reach a different conclusion.

As noted previously, a VIE is consolidated by its primary beneficiary. The primary beneficiary is defined in FIN 46R as the entity that would absorb the majority of the VIE's expected losses or be entitled to receive the majority of the VIE's residual returns (or both).

Significant judgment was involved in determining the primary beneficiary of the Joint Venture. Under FIN 46R, we believe that Olympus and Cytori are "de facto agents" and, together, will absorb more than 50% of the Joint Venture's expected losses and residual returns. Ultimately, we concluded that Olympus, and not Cytori, was the party most closely related with the joint venture and, hence, its primary beneficiary. Our conclusion was based on the following factors:

- The business operations of the Joint Venture will be most closely aligned to those of Olympus (i.e., the manufacture of devices), and

- Olympus controls the Board of Directors, as well as the day-to-day operations of the Joint Venture.

The application of FIN 46R involves substantial judgment, and others may arrive at the conclusion that Cytori should consolidate the Joint Venture. Had we consolidated the Joint Venture, though, there would be no effect on our net loss or shareholders' equity at December 31, 2006 or for the year then ended. However, certain balance sheet and income statement captions would have been presented in a different manner. For instance, we would not have presented a single line item entitled investment in joint venture in our balance sheet, but instead would have performed a line by line consolidation of each of the Joint Venture's accounts into our financial statements.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosure of fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements and, accordingly, does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. We do not believe that the adoption of SFAS 157 will have a significant effect on our consolidated financial statements.

In March 2007, the FASB ratified the consensus reached by the Emerging Issues Task Force on Issue No. 07-3, "Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities" ("EITF 07-3"). EITF 07-3 states that nonrefundable advance payments for future research and development activities should be deferred and capitalized. Such amounts should be recognized as an expense as the goods are delivered or the related services are performed. The guidance is effective for all periods beginning after December 15, 2007. We are currently in the process of evaluating whether the adoption of EITF 07-3 will have a significant effect on our consolidated financial statements.

In February 2007, the FASB issued SFAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities- including an amendment of FASB Statement No. 115" ("SFAS 159"), which permits entities to choose to measure many financial instruments and certain other items at fair value. The provisions of SFAS 159 are effective for financial statements issued for fiscal years beginning after November 15, 2007. We do not believe that the adoption of SFAS 159 will have a significant effect on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We are exposed to market risk related to fluctuations in interest rates and in foreign currency exchange rates.

Interest Rate Exposure

We are not subject to market risk due to fluctuations in interest rates on our long-term obligations as they bear a fixed rate of interest. Our exposure relates primarily to short-term investments. These short-term investments, reported at an aggregate fair market value of $3,795,000 as of June 30, 2007, consist primarily of investments in debt instruments of financial institutions and corporations with strong credit ratings and United States government obligations. These securities are subject to market rate risk as their fair value will fall if market interest rates increase. If market interest rates were to increase immediately and uniformly by 100 basis points from the levels prevailing at June 30, 2007, for example, and assuming average investment duration of seven months, the fair value of the portfolio would not decline by a material amount. We do not use derivative financial instruments to mitigate the risk inherent in these securities. However, we do attempt to reduce such risks by generally limiting the maturity date of such securities, diversifying our investments, and limiting the amount of credit exposure with any one issuer. While we do not always have the intent, we do currently have the ability to hold these investments until maturity and, therefore, believe that reductions in the value of such securities attributable to short-term fluctuations in interest rates would not materially affect our financial position, results of operations, or cash flows. Changes in interest rates would, of course, affect the interest income we earn on our cash balances after re-investment.

Foreign Currency Exchange Rate Exposure

Our exposure to market risk due to fluctuations in foreign currency exchange rates relates primarily to our cash balances in Europe and Japan. Transaction gains or losses resulting from cash balances and revenues have not been significant in the past and we are not engaged in any hedging activity in the Euro, the Yen or other currencies. Based on our cash balances and revenues derived from markets other than the United States of America for the quarter ended June 30, 2007, a hypothetical 10% adverse change in the Euro or Yen against the U.S. dollar would not result in a material foreign currency exchange loss. Consequently, we do not expect that reductions in the value of such sales denominated in foreign currencies resulting from even a sudden or significant fluctuation in foreign exchange rates would have a direct material impact on our financial position, results of operations, or cash flows.

Notwithstanding the foregoing, the indirect effect of fluctuations in interest rates and foreign currency exchange rates could have a material adverse effect on our business, financial condition, and results of operations. For example, foreign currency exchange rate fluctuations may affect international demand for our products. In addition, interest rate fluctuations may affect our prospective customers' buying patterns. Furthermore, interest rate and currency exchange rate fluctuations may broadly influence the United States and foreign economies, resulting in a material adverse effect on our business, financial condition, and results of operations.

Under our Japanese Thin Film agreement with Senko, we would receive payments in the nature of royalties based on Senko's net sales, which would be Yen denominated. We expect such sales to begin in 2007.

Item 4. Controls and Procedures

Christopher J. Calhoun, our Chief Executive Officer, and Mark E. Saad, our Chief Financial Officer, after evaluating the effectiveness of our "disclosure controls and procedures" (as defined in Securities Exchange Act Rule 13a-15(e)), have concluded that as of June 30, 2007, our disclosure controls and procedures are effective. There has been no change in our internal control over financial reporting during the quarter and six months ended June 30, 2007, that has materially affected, or is likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we have been involved in routine litigation incidental to the conduct of our business. As of June 30, 2007, we were not a party to any material legal proceeding. We are not formally a party to the University of Pittsburgh patent litigation. However, we are responsible for reimbursing certain related litigation costs.

Item 1A. Risk Factors

In analyzing our company, you should consider carefully the following risk factors together with all of the other information included in this quarterly report on Form 10-Q. Factors that could adversely affect our business, operating results, and financial condition, as well as adversely affect the value of an investment in our common stock, include those discussed below, as well as those discussed above in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere throughout this quarterly report on Form 10-Q.

We are subject to the following significant risks, among others:

We will need to raise more cash in the future

We have almost always had negative cash flows from operations. Our regenerative cell business will continue to result in a substantial requirement for research and development expenses for several years, during which it could bring in no significant cash and/or revenues. There can be no guarantee that adequate funds for our operations from any additional debt or equity financing, our operating revenues, arrangements with distribution partners, or from other sources will be available when needed or on terms attractive to us. The inability to obtain sufficient funds would require us to delay, scale back, or eliminate some or all of our research or product development programs, manufacturing operations, clinical studies or regulatory activities, or to license third parties to commercialize products or technologies that we would otherwise seek to develop ourselves, thus having a substantial negative effect on our results of operations and financial condition.

We have never been profitable on an operational basis and we expect to have significant operating losses for the next few years

We have incurred net operating losses in each year since we started doing business. As our focus on our regenerative cell technology has increased, these losses have resulted primarily from expenses associated with our research and development activities and general and administrative expenses. Losses related to our development of regenerative cell technology are expected to keep us in a loss position on a consolidated basis for several years. We anticipate that our recurring operating expenses will be at high levels for the next few years, due to the continued need to fund our regenerative cell technology clinical research program as well as additional pre-clinical research.

Our business strategy is high-risk

We are focusing our resources and efforts primarily on our regenerative cell technology and its cash needs for research and development activities. This is a high-risk strategy because there can be no assurance that our regenerative cell technology will ever be developed into commercially viable products (commercial risk), that we will be able to preclude other companies from depriving us of market share and profit margins by selling products based on our inventions and developments (legal risk), that we will be able to successfully manage a company in a different business and on a different scale than we have operated in the past (operational risk), that we will be able to achieve the desired therapeutic results using regenerative cells (scientific risk), or that our cash resources will be adequate to develop the regenerative cell technology until it becomes profitable, if ever (financial risk). We are using our cash in one of the riskiest industries in the economy (strategic risk). This may make our stock an unsuitable investment for some investors.

We must keep our joint venture with Olympus operating smoothly

Our regenerative cell business cannot succeed on the current timelines unless our joint venture collaboration with Olympus goes well. We have given Olympus-Cytori, Inc. an exclusive license to our regenerative cell therapeutic device technology for use in future generation devices. If Olympus-Cytori, Inc. does not successfully develop and manufacture future generation devices for sale to us, we may not be able to commercialize any device or any therapeutic products successfully into the market. In addition, any future disruption in or breakup of our relationship with Olympus would be extremely costly to our reputation, in addition to causing many serious practical problems.

We and Olympus must overcome contractual and cultural barriers as we work together. Our relationship is formally measured by a set of complex contracts, which have not yet been tested in practice. In addition, many aspects of the relationship will be essentially non-contractual and must be worked out between the parties and the responsible individuals over time. The Joint Venture is intended to have a long life, and it is difficult to maintain cooperative relationships over a long period of time from a far distance in the face of various kinds of change. Cultural differences, including a language barrier to some degree, may affect the efficiency of the relationship as well.

Olympus-Cytori, Inc. is 50% owned by us and 50% owned by Olympus. By contract, each side must consent before any of a wide variety of important business actions can occur. This situation possesses a risk of potentially time-consuming and difficult negotiations which could at some point delay the Joint Venture from pursuing its business strategies.

Olympus is entitled to designate the Joint Venture's chief executive officer and a majority of its board of directors, which means that day-to-day decisions which are not subject to a contractual veto will essentially be controlled by Olympus. In addition, Olympus-Cytori, Inc. will need more money than its initial capitalization in order to finalize development of and production of the future generation devices. If we are unable to help provide future financing for Olympus-Cytori, Inc., our relative equity interest in Olympus-Cytori, Inc. may decrease.

Furthermore, under a License/Joint Development Agreement among Olympus-Cytori, Inc., Olympus, and us, Olympus will have a primary role in the development of Olympus-Cytori, Inc.'s future generation devices. Although Olympus has extensive experience in developing medical devices, this arrangement will result in a reduction of our control over the development and manufacturing of the future generation devices.

We have a limited operating history; our operating results and stock price, like those of all emerging life science companies, can be volatile

Our prospects must be evaluated in light of the risks and difficulties frequently encountered by emerging companies and particularly by such companies in rapidly evolving and technologically advanced fields such as the biotechnology and medical device fields. Due to our limited operating history, and the development stage status of our regenerative cell business, comparisons of our year-to-year operating results are not necessarily meaningful and the results for any periods should not necessarily be relied upon as an indication of future performance. Operating results will also be affected by our transition away from our revenue-generating medical device business and the focus of the vast majority of our resources into the development of the regenerative cell business. All of our recent product revenues have come from our spine and orthopedics bioresorbable implants product line, which we sold in May 2007.

From time to time, we have tried to influence our investors' expectations as to our operating results by periodically announcing financial guidance. However, we have in the past been forced to revise or withdraw such guidance due to lack of visibility and predictability of product demand.

We are vulnerable to competition and technological change, and also to physicians' inertia

We compete with many domestic and foreign companies in developing our technology and products, including biotechnical, medical device, pharmaceutical, and biopharmaceutical companies. Many of our competitors and potential competitors have substantially greater financial, technological, research and development, marketing, and personnel resources than we do. There can be no assurance that our competitors will not succeed in developing alternative technologies and products that are more effective, easier to use, or more economical than those which we have developed or are in the process of developing, or that would render our technology and products obsolete and non-competitive in these fields. In general, we may not be able to preclude other companies from developing and marketing competitive regenerative cell therapies that are similar to ours or perform similar functions.

These competitors may also have greater experience in developing therapeutic treatments, conducting clinical trials, obtaining regulatory clearances or approvals, manufacturing and commercializing therapeutic products. It is possible that certain of these competitors may obtain patent protection, approval, or clearance from the FDA or achieve commercialization earlier than we, any of which could have a substantial negative effect on our business. Finally, Olympus and our other partners might pursue parallel development of other technologies or products, which may result in a partner developing additional products that will compete with our products.

We also compete with other types of regenerative cell therapies, such as bone marrow-derived cell therapies and potentially embryonic-derived therapies. Doctors have historically been slow to adopt new technologies such as ours, whatever the merits, when older technologies continue to be supported by established providers. Overcoming such inertia often requires very significant marketing expenditures or definitive product superiority.

We expect physicians' inertia and skepticism to also be a significant barrier as we attempt to gain market penetration with our future regenerative cell products. We believe we will need to finance lengthy time-consuming clinical studies (so as to provide convincing evidence of the medical benefit) in order to overcome this inertia and skepticism.

Our regenerative cell technology products are pre-commercialization, which subjects us to development and marketing risks

We are in a relatively early stage of the path to commercialization with many of our products. We believe that our long-term viability and growth will depend in large part on our ability to develop commercial quality cell processing devices and useful procedure-specific consumables, and to establish the safety and efficacy of our therapies through clinical trials and studies. We are presently pursuing therapies for cardiovascular disease as well as new approaches for aesthetic and reconstructive surgery, gastrointestinal disorders and spine and orthopedic conditions. There can be no assurance that our development programs will be successfully completed or that required regulatory clearances or approvals will be obtained on a timely basis, if at all.

There is no proven path for commercializing our regenerative cell technology in a way to earn a durable profit commensurate with the medical benefit. Although we intend to commercialize aesthetic and reconstructive surgery and our regenerative cell banking platform in 2008, additional market opportunities for our cell-related products and/or services are at least two to five years away.

Moreover, the successful development and market acceptance of our technologies and products are subject to inherent developmental risks, including failure of inventive imagination, ineffectiveness or lack of safety, unreliability, failure to receive necessary regulatory clearances or approvals, high commercial cost, and preclusion or obsolescence resulting from third parties' proprietary rights or superior or equivalent products, and competition from copycat products, as well as general economic conditions affecting purchasing patterns. There can be no assurance that we or our partners will be able to successfully develop and commercialize our technologies or products, or that our competitors will not develop competing technologies that are less expensive or otherwise superior to ours. The failure to successfully develop and market our new regenerative cell technologies would have a substantial negative effect on our results of operations and financial condition.

The timing and amount of Thin Film revenues from Senko are uncertain

The sole remaining product line in our MacroPore Biosurgery segment is our Japan Thin Film business. Our right to receive royalties from Senko, and to recognize certain deferred revenues, depends on the timing of MHLW approval for commercialization of the product in Japan. We currently expect this to occur in 2007, but we have no control over this timing and our expectations have fallen short before. Also, even after commercialization, we will be dependent on Senko, our exclusive distributor, to increase product sales in Japan.

There is a risk that we could experience with Senko some of the same problems we experienced in our previous relationship with Medtronic, which was the exclusive distributor for our former bioresorbable spine and orthopedic implant product line.

We have limited manufacturing experience

We have no experience in manufacturing the Celution™ System at a commercial level, and although Olympus is a highly capable and experienced manufacturer of medical devices, there can be no guarantee that the Olympus-Cytori joint venture will be able to successfully develop and manufacture the Celution™ System in a manner that is cost-effective or commercially viable, or that development and manufacturing capabilities might not take much longer than currently anticipated to be ready for the market.

In the event that the Olympus-Cytori joint venture is not successful, Cytori may not have the resources or ability to self-manufacture commercially viable devices, and in any event this failure may substantially extend the time it would take for us to bring a commercial device to market. This makes us significantly dependant on the continued dedication and skill of Olympus for the successful development of the Celution™ System.

In addition, as a company we have limited experience in manufacturing the type of cell-related therapeutic products which we intend to introduce in the future.

We may not be able to protect our proprietary rights

Our success depends in part on whether we can obtain additional patents, maintain trade secret protection, and operate without infringing on the proprietary rights of third parties.

Our recently amended regenerative cell technology license agreement with the Regents of the University of California contains certain developmental milestones, which if not achieved could result in the loss of exclusivity or loss of the license rights. The loss of such rights could impact our ability to develop certain regenerative cell technology products. Also, our power as licensee to successfully use these rights to exclude competitors from the market is untested. In addition, further legal risk arises from a lawsuit filed by the University of Pittsburgh naming all of the inventors who had not assigned their ownership interest in Patent 6,777,231 to the University of Pittsburgh, seeking a determination that its assignors, rather than the University of California's assignors, are the true inventors of Patent 6,777,231. We are the exclusive, worldwide licensee of the University of California's rights under this patent, which relates to adult stem cells isolated from adipose tissue that can differentiate into two or more of a variety of cell types. If the University of Pittsburgh wins the lawsuit, our license rights to this patent could be nullified or rendered non-exclusive with respect to any third party that might license rights from the University of Pittsburgh, and our regenerative cell strategy could be impacted.

On August 3, 2007, the United States Patent and Trademark Office issued a "Revised Decision (Correction of Inventorship)" specifying that the correct inventorship of Patent 6,777,231 is only UC's assignees. On August 9, 2007, the United States District Court, without the benefit of the Patent Office Inventorship Decision, granted the University of Pittsburgh's motion for Summary Judgment in part, determining that the University of Pittsburgh's assignees were properly named as inventors on Patent 6,777,231, and that all other inventorship issues shall be determined according to the facts presented at trial.

There can be no assurance that any of the pending patent applications will be approved or that we will develop additional proprietary products that are patentable. There is also no assurance that any patents issued to us will provide us with competitive advantages, will not be challenged by any third parties, or that the patents of others will not prevent the commercialization of products incorporating our technology. Furthermore, there can be no guarantee that others will not independently develop similar products, duplicate any of our products, or design around our patents.

Our commercial success will also depend, in part, on our ability to avoid infringing on patents issued to others. If we were judicially determined to be infringing on any third-party patent, we could be required to pay damages, alter our products or processes, obtain licenses, or cease certain activities. If we are required in the future to obtain any licenses from third parties for some of our products, there can be no guarantee that we would be able to do so on commercially favorable terms, if at all. U.S. patent applications are not immediately made public, so we might be surprised by the grant to someone else of a patent on a technology we are actively using. As noted above as to the University of Pittsburgh lawsuit, even patents issued to us or our licensors might be judicially determined to belong in full or in part to third parties.

Litigation, which would result in substantial costs to us and diversion of effort on our part, may be necessary to enforce or confirm the ownership of any patents issued or licensed to us, or to determine the scope and validity of third-party proprietary rights. If our competitors claim technology also claimed by us and prepare and file patent applications in the United States of America, we may have to participate in interference proceedings declared by the U.S. Patent and Trademark Office or a foreign patent office to determine priority of invention, which could result in substantial costs to and diversion of effort, even if the eventual outcome is favorable to us.

Any such litigation or interference proceeding, regardless of outcome, could be expensive and time-consuming. We have been incurring substantial legal costs as a result of the University of Pittsburgh lawsuit, and our president, Marc Hedrick, is a named individual defendant in that lawsuit because he is one of the inventors identified on the patent. As a named inventor on the patent, Marc Hedrick is entitled to receive from the Regents of the University of California up to 7% of royalty payments made by a licensee (us) to the Regents of the University of California. This agreement was in place prior to his employment with us.

In addition to patents, which alone may not be able to protect the fundamentals of our regenerative cell business, we also rely on unpatented trade secrets and proprietary technological expertise. Our intended future cell-related therapeutic products, such as consumables, are likely to fall largely into this category. We rely, in part, on confidentiality agreements with our partners, employees, advisors, vendors, and consultants to protect our trade secrets and proprietary technological expertise. There can be no guarantee that these agreements will not be breached, or that we will have adequate remedies for any breach, or that our unpatented trade secrets and proprietary technological expertise will not otherwise become known or be independently discovered by competitors.

Failure to obtain or maintain patent protection, or protect trade secrets, for any reason (or third-party claims against our patents, trade secrets, or proprietary rights, or our involvement in disputes over our patents, trade secrets, or proprietary rights, including involvement in litigation), could have a substantial negative effect on our results of operations and financial condition.

We may not be able to protect our intellectual property in countries outside the United States

Intellectual property law outside the United States is uncertain and in many countries is currently undergoing review and revisions. The laws of some countries do not protect our patent and other intellectual property rights to the same extent as United States laws. We currently have pending patent applications in Europe, Australia, Japan, Canada, China, Korea, and Singapore, among others.

We are, and Olympus-Cytori, Inc. will be, subject to intensive FDA regulation

As newly developed medical devices, our and Olympus-Cytori's regenerative cell harvesting, isolation and delivery devices must receive regulatory clearances or approvals from the FDA and, in many instances, from non-U.S. and state governments prior to their sale. Our and Olympus-Cytori's current and future regenerative cell harvesting, isolation and delivery devices are subject to stringent government regulation in the United States by the FDA under the Federal Food, Drug and Cosmetic Act. The FDA regulates the design/development process, clinical testing, manufacture, safety, labeling, sale, distribution, and promotion of medical devices and drugs. Included among these regulations are pre-market clearance and pre-market approval requirements, design control requirements, and the Quality System Regulations/Good Manufacturing Practices. Other statutory and regulatory requirements govern, among other things, establishment registration and inspection, medical device listing, prohibitions against misbranding and adulteration, labeling and post-market reporting.

The regulatory process can be lengthy, expensive, and uncertain. Before any new medical device may be introduced to the United States of America market, the manufacturer generally must obtain FDA clearance or approval through either the 510(k) pre-market notification process or the lengthier pre-

market approval application ("PMA") process. It generally takes from three to 12 months from submission to obtain 510(k) pre-market clearance, although it may take longer. Approval of a PMA could take four or more years from the time the process is initiated. The 510(k) and PMA processes can be expensive, uncertain, and lengthy, and there is no guarantee of ultimate clearance or approval. We expect that some of our future products under development as well as Olympus-Cytori's will be subject to the lengthier PMA process. Securing FDA clearances and approvals may require the submission of extensive clinical data and supporting information to the FDA, and there can be no guarantee of ultimate clearance or approval. Failure to comply with applicable requirements can result in application integrity proceedings, fines, recalls or seizures of products, injunctions, civil penalties, total or partial suspensions of production, withdrawals of existing product approvals or clearances, refusals to approve or clear new applications or notifications, and criminal prosecution.

Medical devices are also subject to post-market reporting requirements for deaths or serious injuries when the device may have caused or contributed to the death or serious injury, and for certain device malfunctions that would be likely to cause or contribute to a death or serious injury if the malfunction were to recur. If safety or effectiveness problems occur after the product reaches the market, the FDA may take steps to prevent or limit further marketing of the product. Additionally, the FDA actively enforces regulations prohibiting marketing and promotion of devices for indications or uses that have not been cleared or approved by the FDA.

There can be no guarantee that we will be able to obtain the necessary 510(k) clearances or PMA approvals to market and manufacture our other products in the United States of America for their intended use on a timely basis, if at all. Delays in receipt of or failure to receive such clearances or approvals, the loss of previously received clearances or approvals, or failure to comply with existing or future regulatory requirements could have a substantial negative effect on our results of operations and financial condition.

To sell in international markets, we will be subject to intensive regulation in foreign countries

In cooperation with our distribution partners, we intend to market our current and future products both domestically and in many foreign markets. A number of risks are inherent in international transactions. In order for us to market our products in Europe, Canada, Japan and certain other non-U.S. jurisdictions, we need to obtain and maintain required regulatory approvals or clearances and must comply with extensive regulations regarding safety, manufacturing processes and quality. For example, we still have not obtained regulatory approval for our Thin Film products in Japan. These regulations, including the requirements for approvals or clearances to market, may differ from the FDA regulatory scheme. International sales also may be limited or disrupted by political instability, price controls, trade restrictions and changes in tariffs. Additionally, fluctuations in currency exchange rates may adversely affect demand for our products by increasing the price of our products in the currency of the countries in which the products are sold.

There can be no assurance that we will obtain regulatory approvals or clearances in all of the countries where we intend to market our products, or that we will not incur significant costs in obtaining or maintaining foreign regulatory approvals or clearances, or that we will be able to successfully commercialize current or future products in various foreign markets. Delays in receipt of approvals or clearances to market our products in foreign countries, failure to receive such approvals or clearances or the future loss of previously received approvals or clearances could have a substantial negative effect on our results of operations and financial condition.

We and/or the Joint Venture have to maintain quality assurance certification and manufacturing approvals

The manufacture of our Celution™ System for regenerative cells will be, and the manufacture of any future cell-related therapeutic products would be, subject to periodic inspection by regulatory authorities and distribution partners. The manufacture of devices and products for human use is subject to regulation and inspection from time to time by the FDA for compliance with the FDA's Quality System Regulation ("QSR") requirements, as well as equivalent requirements and inspections by state and non-U.S. regulatory authorities. There can be no guarantee that the FDA or other authorities will not, during the course of an inspection of existing or new facilities, identify what they consider to be deficiencies in our compliance with QSRs or other requirements and request, or seek, remedial action.

Failure to comply with such regulations or a potential delay in attaining compliance may adversely affect our manufacturing activities and could result in, among other things, injunctions, civil penalties, FDA refusal to grant pre-market approvals or clearances of future or pending product submissions, fines, recalls or seizures of products, total or partial suspensions of production, and criminal prosecution. There can be no assurance that we will be able to obtain additional necessary regulatory approvals or clearances on a timely basis, if at all. Delays in receipt of or failure to receive such approvals or clearances, or the loss of previously received approvals or clearances could have a substantial negative effect on our results of operations and financial condition.

We depend on a few key officers

Our performance is substantially dependent on the performance of our executive officers and other key scientific staff, including Christopher J. Calhoun, our Chief Executive Officer, and Marc Hedrick, MD, our President. We rely upon them for strategic business decisions and guidance. We believe that our future success in developing marketable products and achieving a competitive position will depend in large part upon whether we can attract and retain additional qualified management and scientific personnel. Competition for such personnel is intense, and there can be no assurance that we will be able to continue to attract and retain such personnel. The loss of the services of one or more of our executive officers or key scientific staff or the inability to attract and retain additional personnel and develop expertise as needed could have a substantial negative effect on our results of operations and financial condition. Two executive officers left us in 2006, one in connection with a summer 2006 reduction of our headcount by 18%.

Companies which make personnel cuts sometimes find the resulting loss of experience and lack of coverage can cause important business problems.

We may not have enough product liability insurance

The testing, manufacturing, marketing, and sale of our regenerative cell products involve an inherent risk that product liability claims will be asserted against us, our distribution partners, or licensees. There can be no guarantee that our clinical trial and commercial product liability insurance is adequate or will continue to be available in sufficient amounts or at an acceptable cost, if at all. A product liability claim, product recall, or other claim, as well as any claims for uninsured liabilities or in excess of insured liabilities, could have a substantial negative effect on our results of operations and financial condition. Also, well-publicized claims could cause our stock to fall sharply, even before the merits of the claims are decided by a court.

Our charter documents contain anti-takeover provisions and we have adopted a Stockholder Rights Plan to prevent hostile takeovers

Our Amended and Restated Certificate of Incorporation and Bylaws contain certain provisions that could prevent or delay the acquisition of the Company by means of a tender offer, proxy contest, or otherwise. They could discourage a third party from attempting to acquire control of the Company, even if such events would be beneficial to the interests of our stockholders. Such provisions may have the effect of delaying, deferring, or preventing a change of control of the Company and consequently could adversely affect the market price of our shares. Also, in 2003 we adopted a Stockholder Rights Plan, of the kind often referred to as a poison pill. The purpose of the Stockholder Rights Plan is to prevent coercive takeover tactics that may otherwise be utilized in takeover attempts. The existence of such a rights plan may also prevent or delay a change in control of the Company, and this prevention or delay adversely affect the market price of our shares.

We pay no dividends

We currently do not intend to pay any cash dividends for the foreseeable future.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

No further disclosure required

Item 3. Defaults Upon Senior Securities

None

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5.

Other Information

Material Agreements

None

Properties

On May 24, 2005, we entered into a lease for 91,000 square feet located at 3020 and 3030 Callan Road, San Diego, California. We moved the majority of our operations to this new facility during the second half of 2005 and the first quarter of 2006. The agreement bears rent at a rate of $1.15 per square foot, with annual increases of 3%. The lease term is 57 months, commencing on October 1, 2005 and expiring on June 30, 2010.

Our lease on the facility located at 6740 Top Gun Street, San Diego, California was amended and terminated on December 31, 2006. We will continue to occupy a portion of the building and pay rent to the new lessee until August 31, 2007. We also lease 4,027 square feet of office space located at 9-3 Otsuka 2-chome, Bunkyo-ku, Tokyo, Japan. The agreement bears rent at a rate of $3.66 per square foot, expiring on November 30, 2007.

On the properties stated above, we pay an aggregate of approximately $149,000 in rent per month.

Staff

As of June 30, 2007, we had 140 full-time equivalent employees, comprised of 5 employees in manufacturing, 88 employees in research and development, 7 employees in sales and marketing, and 40 employees in management and finance and administration. From time to time, we also employ independent contractors to support our administrative organizations. Our employees are not represented by any collective bargaining unit and we have never experienced a work stoppage. A breakout by segment is as follows:

	Regenerative Cell Technology	MacroPore Biosurgery	Corporate	Total
Manufacturing	—	5	—	5
Research & Development	87	1	—	88
Sales and Marketing	7	—	—	7
General & Administrative	—	—	40	40
Total	94	6	40	140

Voluntary Disclosure

On August 13, 2007, we entered into an exclusive distribution and supply agreement with Green Hospital Supply, Inc.to commercialize our StemSource™ cell bank in Japan. The StemSource™ cell bank is an automated platform that incorporates the use of our Celution™ System and disposables to enable hospitals and clinics in Japan to harvest, process and store regenerative cells from a patient’s adipose tissue for potential later use. This enterprise is subject to all of the risks associated with any new business venture, including risks relating to market acceptance.

Item 6. Exhibits

2.5	Asset Purchase Agreement, dated May 30, 2007, between Cytori Therapeutics, Inc. and MacroPore Acquisition Sub, Inc.
10.47	Consulting Agreement, dated May 3, 2007, between Cytori Therapeutics, Inc. and Marshall G. Cox
15.1	Letter re unaudited interim financial information.
31.1	Certification of Chief Executive Officer Pursuant to Securities Exchange Act Rule 13a-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Securities Exchange Act Rule 13a-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification pursuant to 18 U.S.C. Section 1350/ Securities Exchange Act Rule 13a-14(b), as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Index

SIGNATURES

Pursuant to the requirements 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, in San Diego, California, on August 14, 2007.

CYTORI THERAPEUTICS, INC.

By: /s/ Christopher J. Calhoun
Christopher J. Calhoun
Chief Executive Officer

Dated: August 14, 2007

By: /s/ Mark E. Saad
Mark E. Saad
Chief Financial Officer

Dated: August 14, 2007

Exhibit 2.5

ASSET PURCHASE AGREEMENT

THIS ASSET PURCHASE AGREEMENT (this "**Agreement**") is made on this 30th day of May 2007, by and between Cytori Therapeutics, Inc., a Delaware corporation (the "**Company**"), and MacroPore Acquisition Sub, Inc., a Delaware corporation ("**Buyer**").

WHEREAS, the Company is engaged in the business of developing, manufacturing, commercializing and marketing technology and products in connection with bioresorbable implants in its conduct of the Business (as defined in **Section 7.10**);

WHEREAS, the Company desires to sell to Buyer, and Buyer desires to purchase from the Company, certain assets used in the Business, subject to the terms and conditions set forth below; and

WHEREAS, certain capitalized terms have the meanings respectively indicated in **Section 7.10** herein.

NOW THEREFORE, in consideration of the mutual covenants of the parties set forth in this Agreement and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I

PURCHASE AND SALE OF ASSETS

1.1 Assets.

(a) On the terms and subject to the conditions set forth in this Agreement, at the Closing, the Company shall sell, transfer and deliver to Buyer, free and clear of all liens, hypothecations, mortgages, charges, security interests, pledges or other encumbrances or adverse claims or interests of any nature ("**Liens**"), and Buyer shall purchase from the Company, all of the Company's right, title and interest as of the Closing Date in and to the following assets that are primarily used in, relate to or arise out of the conduct of the Business (collectively, the "**Assets**"):

(i) Equipment. All machinery, equipment, furniture, supplies, tools, dies, molds, fixtures and all other tangible or movable personal property included under the "Equipment" heading on the Specified Assets Schedule 1.1(a)(i), including, but not limited to, the Deposit Assets (collectively, the "**Equipment**");

(ii) Inventory and Supplies. All inventory of the Company used in connection with the Business and included under "Inventory" on the Specified Assets Schedule 1.1(a)(ii), including, without limitation, raw materials, work-in-process, finished goods, merchandise for resale, spare parts, packaging and shipping materials and other Business manufacturing supplies, whether or not located at the Company's principal place of business (collectively, the "**Inventory**");

(iii) Contracts. All rights, benefits, duties and obligations that the Company may have under the Contracts or portions thereof listed on Schedule 1.1(a)(iii) hereto (the "**Assumed Contracts**");

(iv) Proprietary Rights. All intellectual property, confidential information, and proprietary information in the world owned or used by the Company primarily in connection with the Business including, specifically as follows (collectively, "**Proprietary Rights**"):

(a) all patents, patent applications, patent disclosures and inventions (whether or not patentable and whether or not reduced to practice) as listed on Schedule 1.1(a)(iv)(a) hereto;

(b) any trademarks, service marks, trade dress, trade names and corporate names specifically listed on Schedule 1.1(a)(iv)(b) hereto;

(c) all registered and unregistered statutory and common law copyrights used primarily in the conduct of the Business;

(d) all registrations, applications, extensions and renewals for any of the foregoing;

(e) all trade secrets, confidential information, ideas, formulae, compositions, know-how, manufacturing and production processes and techniques, research and development information, drawings, specifications, designs, plans, improvements, proposals, technical and computer data, databases, documentation and software, financial, business and marketing plans, and customer and supplier lists and related information used in the conduct of the Business;

(f) all agreements, commitments, contracts, understandings, licenses, assignments or indemnities relating or pertaining to an asset, property or right of the character described in the preceding clauses to which the Company is a party;

(g) all licenses or agreements pertaining to mailing lists, know-how, trade secrets, inventions, disclosures or uses of ideas used in or relating to the Business to which the Company is a party;

(h) all correspondence and memoranda between the Company and its intellectual property counsel relating to Proprietary Rights, including without limitation all documentation related to the protection or analysis thereof; and

(i) all other intellectual property, confidential information and proprietary rights used primarily in connection with the Business;

(v) Licenses, Permits and Approvals. All rights of the Company in and to the Permits identified on Schedule 1.1(a)(v), including, without limitation, specified FDA approvals, to the extent assignable; provided however, that all rights to regulatory approvals for the Company's thin film (SurgiWrap/Hydrosorb Shield) shall be subject to the limitations and obligations mentioned in the side letters attached as Exhibit A to Schedule 1.1(a)(v);

(vi) Claims. All warranties, guarantees, refunds (other than tax refunds), covenants, indemnities and the like, with respect to the Inventory and other Assets transferred hereunder;

(vii) Books and Records. The books and records relating primarily to the operation of the Business, including all records, documentation of research and development, files, papers, sales and purchase and other correspondence, but excluding all general corporate records and personnel files of the Company;

(viii) Customer Information. All customer information, distributor information, sales representative information, sales contact management information (from both employees and contract agents), sales ledgers and records, in each case as specifically related to the Business and in whatever form; and

(ix) Domain Names. The websites and internet domain names relating to the Business as listed on Schedule 1.1(a)(ix), and the exclusive right to display, prepare, reproduce, create derivative works based on, and operate (as applicable) the same.

(b) Notwithstanding the foregoing, the following assets of the Company and all assets described on the Excluded Assets Schedule 1.1(b) shall be retained by the Company and are expressly excluded from the purchase and sale contemplated by this Agreement (collectively, the "**Excluded Assets**"):

(i) Cash. All cash and cash equivalents of the Company;

(ii) This Agreement. The Company's rights pursuant to this Agreement and the Transaction Documents;

(iii) Nonassignable Permits. Any Permits that may not be transferred without the consent, novation, waiver or approval of another Person and for which such consent, novation, waiver or approval has not been obtained;

(iv) Employee Benefit Plans. All monies, rights and other assets (including any insurance policy, annuity contract or trust) maintained under, pursuant to or in direct connection with any Employee Benefit Plan;

(v) Excluded Contracts. All rights and benefits that the Company may have under any Contracts that are not Assumed Contracts;

(vi) Insurance. All insurance policies of the Company and (except as otherwise set forth in **Section 1.1(a)(vi)**), all claims, rights and proceeds thereunder; and

(vii) Accounts Receivable. All accounts receivable, notes or other indebtedness of any Person held by the Company.

(c) It is understood that all specifications, drawings, samples, designs, software, and other items and information furnished by Medtronic to the Company remain Medtronic's property to the same extent that such items were owned by Medtronic (rather than the Company) immediately prior to the Closing, and such Assets shall be delivered to Buyer hereunder, subject to any rights of Medtronic therein (whether or not specifically disclosed by the Company to Buyer), notwithstanding anything in this Agreement to the contrary.

1.2 Assumption of Liabilities»

. Notwithstanding anything to the contrary contained in this Agreement or any Transaction Document, and regardless of whether such Liability is disclosed in this Agreement, in any of the Transaction Documents, on any Schedule hereto or thereto or otherwise, and regardless of Buyer's or any of its directors', officers', employees' or agents' knowledge or awareness of any Liability, whether learned in connection with Buyer's due diligence investigation of the Business or otherwise, Buyer will not assume, agree to pay, perform or discharge or in any way be responsible for any Liabilities (the "**Excluded Liabilities**"), except that Buyer will assume following the Closing the obligations arising under the Assumed Contracts, including any royalties that are due there under after the Closing (the "**Assumed Liabilities**"); provided, however, that any Liability relating to or arising from any breach, or event, circumstance or condition that with notice, lapse of time or both would constitute or result in a breach, by the Company, on or before the Closing Date, of any of its obligations thereunder shall be an Excluded Liability. Without limiting the generality of the foregoing, Buyer is not assuming or agreeing to pay, perform or

discharge or in any way be responsible for, any Excluded Liabilities, which shall include, but not be limited to: (i) all Indebtedness, (ii) all Company Taxes, (iii) all Liabilities related to employee compensation and employee benefit plans or obligations of the Company (including severance, non-compete payments, benefits, deferred compensation, continuation coverage required under COBRA for each individual who is or becomes an "M & A Qualified Beneficiary" (as such term is defined in the Treas. Reg. §54.4980B-9 and workers' compensation claims) as a result of the consummation of the transactions contemplated this Agreement), (iv) all Liabilities related to litigation and environmental matters with respect to the Assets for any period (or portion thereof) ending on or before the Closing Date, (v) all Liabilities relating to or arising out of any transaction contemplated by this Agreement or the Transaction Documents, (vi) any Liabilities with respect to any Products, or (vii) any other liabilities or obligations associated with the ownership of the Assets on or prior to Closing or the stockholders of the Company at any time.

1.3 Conveyance»

. At the Closing, the Company and Buyer shall execute and deliver a Bill of Sale, Assignment and Assumption Agreement (the "**Bill of Sale**"), pursuant to which the Company shall convey to the Buyer the Assets and the Buyer shall assume the Assumed Liabilities.

ARTICLE II

CONSIDERATION AND MANNER OF PAYMENT

2.1 Purchase Price»

. The purchase price (the "**Purchase Price**") to be paid by Buyer for the Assets, and the rights and benefits conferred hereunder, shall be Three Million One Hundred Seventy Five Thousand Dollars ($3,175,000), which amount shall be payable by Buyer to the Company at Closing, by wire transfer of immediately available funds to an account or accounts specified by the Company in writing, in an amount equal to the Purchase Price minus the Deposit Amount (the "**Cash Payment**").

2.2 Purchase Price Allocation»

. Buyer shall prepare an allocation of the Purchase Price (along with the Assumed Liabilities and any other items constituting consideration for purposes of Section 1060 of the Code), taking into account any adjustments made thereto pursuant to this Agreement, among the Assets and the covenants and agreements set forth in **Section 6.5** in accordance with Section 1060 of the Code and the Treasury Regulations thereunder (and any similar provision of state, local or foreign law, as appropriate). Buyer shall deliver a proposal regarding such allocation to the Company within sixty (60) days after the Closing (the "**Proposed Allocation**"). Upon receipt of the Proposed Allocation, the Company shall deliver to Buyer within fifteen (15) days a written notice (the "**Company Response**") which shall specify either that the Company agrees with the Proposed Allocation as final or else which portion(s) of the Proposed Allocation the Company does not agree with in its good faith determination; provided that if the Company shall not respond within such fifteen (15) day period, it will be deemed to have consented to the Proposed Allocation as final. Upon receipt of the Company Response, if any, Buyer and the Company shall in good faith attempt to come to an agreement over any disputes within fifteen (15) days following Buyer's receipt of the Company Response. If Buyer and the Company cannot come to an agreement within such period, the matter shall be referred to Deloitte & Touche LLP, which firm shall make a final determination as to the proper allocation within fifteen (15) days of submission of the matter to such firm. The final allocation to be delivered pursuant to the terms of this **Section 2.2** shall be binding upon the Company and Buyer for all purposes. In the event an adjustment to the Purchase Price (or any item constituting consideration for purposes of Section 1060 of the Code) is made pursuant to this Agreement, the final allocation of the Purchase Price shall be revised accordingly by Buyer and delivered to the Company as soon as reasonably practicable. Buyer, the Company and each of their respective Affiliates shall take all actions and properly and timely file all Tax Returns (including, but not limited to IRS Form 8594 (Asset Acquisition Statement)) consistent with such allocation and shall not take any action inconsistent therewith. The Company and its Affiliates shall timely and properly prepare, execute, file and deliver all such documents, forms and other information as Buyer may reasonably request to prepare such allocation.

ARTICLE III

REPRESENTATIONS AND WARRANTIES OF THE COMPANY

As a material inducement to Buyer to enter into this Agreement, the Company makes to Buyer the representations and warranties set forth in this **Article III**, which representations and warranties are made and shall be true and correct with respect to the Business as of the date hereof.

3.1 Authority»

. The Company has full power, right and authority to enter into and perform its obligations under this Agreement and each of the Company Transaction Documents. The execution, delivery and performance of this Agreement and each of the Company Transaction Documents and the consummation of the transactions contemplated hereby have been duly and validly authorized by all requisite action in accordance with applicable Rules, and no other proceedings are necessary to authorize the execution, delivery and performance of this Agreement and each of the Company Transaction Documents. This Agreement and each of the Company Transaction Documents have been duly executed and delivered by the Company and constitute the valid and

binding obligations of the Company and are enforceable against the Company in accordance with their respective terms, except as may be limited by bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium or other laws of general application relating to the enforcement of creditors' rights and general equitable principles (whether considered in a proceeding in equity or at law).

3.2 Organization and Qualification of the Company»

. The Company is a corporation duly organized, validly existing, and in good standing under the laws of the State of Delaware. The Company has full power and authority to own or hold under lease the properties and assets it now owns or holds under lease in connection with the Business.

3.3 Transaction Not a Breach»

. Neither the execution and delivery of this Agreement or any Company Transaction Document by the Company nor the performance by the Company of the transactions contemplated hereby or thereby will:

(a) violate or conflict with or result in a breach of any provision of any law, statute, rule, regulation, requirement, approval, order, permit, judgment, injunction, decree or other decision (collectively, "**Rules**") of any court or other tribunal or any Governmental Authority binding on the Company or its properties, or conflict with or result in the breach of any of the terms, conditions or provisions thereof;

(b) violate or conflict with or constitute (with or without notice or lapse of time or both) a default under the organizational or governing documents of the Company or any Permit or Contract;

(c) constitute an event which would permit any party to terminate, modify, or accelerate the maturity of any Indebtedness or other obligation under any Contract;

(d) result in the creation or imposition of any Lien upon the Assets; or

(e) require any Permit, authorization, consent, approval, exemption, or other action by or notice to any Person, court or administrative or Governmental Authority pursuant to any Rules.

3.4 No Consent Required»

. Except as set forth on Schedule 3.4, no consent, approval, order or authorization of, or declaration, filing or registration with, any Person or Governmental Authority is required to be made or obtained by the Company in connection with the authorization, execution, delivery, performance or lawful completion of this Agreement, the other Company Transaction Documents or the transactions contemplated hereby.

3.5 Financial Information.

(a) Schedule 3.5 sets forth the amount of Net Revenue by product line for each completed fiscal quarter during the years 2004 through 2007. "**Net Revenue**" means the gross revenue received by the Company or any Affiliate thereof in connection with the Business, minus (i) any refunds, credits or allowances actually given or credited to any party due to rejections, defects or returns of product, (ii) any discounts or rebates actually given or credited by the Company or any Affiliate thereof, (iii) any Taxes, duties or other governmental charges imposed on, and paid by the Company and its Affiliates, in connection with the importation, exportation, use or sale of product, and (iv) any freight, postage or insurance charges incurred by the Company or its Affiliates in connection with product.

(b) Except for the potential effects of the transaction contemplated by this Agreement which has been known to Company's sole customer, and the recent termination of certain real property leases by Company connected to the operations of the Business, there has not been any material change to the value of the Assets from that set forth in the financial information provided by the Company to Buyer in the course of Buyer's due diligence investigation of the Business.

3.6 Absence of Undisclosed Liabilities»

. The Company has no Liabilities in connection with the Assets arising out of transactions entered into on or prior to the date hereof, or any transaction, series of transactions, action or inaction occurring on or prior to the date hereof, or any state of facts or condition existing on or prior to the date hereof (regardless of when such Liability is asserted), including, but not limited to, Liabilities on account of Taxes or governmental charges or penalties, interest or fines thereon or in respect thereof, except for the Assumed Liabilities.

3.7 Assets.

(a) Title. The Company has the exclusive right to possess and convey, and upon the consummation of the transactions contemplated by this Agreement, the Company will have conveyed and Buyer will be vested with, good and marketable title and interest in and to the Assets, free and clear of all Liens (other than Permitted Liens). Assuming the Buyer enters into arrangements with Medtronic that are materially equivalent to the Medtronic Supply Agreement, and assuming the Buyer has its own facilities and personnel that are materially equivalent to those with which the Company operates the Business, and assuming Buyer does not need any of those patents included on the Excluded Assets Schedule 1.1(b), the Assets are sufficient to enable Buyer to conduct the Business immediately after the Closing in materially the same manner as conducted by the Company. Other than as set forth on Schedule 3.7(a), no Person (other than the Company) including, without limitation, any Subsidiary or Affiliate of the Company, owns or has any right to the use or possession of any tangible personal property included in the Assets, other than lessors and licensors of such tangible personal property constituting leasehold interests or licenses.

(b) Inventories. The Inventory: (i) consists of items of a quality and quantity useable or saleable in the ordinary course of business, (ii) is the property of the Company free and clear of any Lien and (iii) is located at the real property leased by the Company. None of the Inventory is held by the Company on consignment. The Company has no liability to any consignor with respect to the prior sale of any inventory held at any time under consignment or similar arrangement.

(c) Condition and Location. Schedule 3.7(c) lists all maintenance records of the Company relating to the tangible assets that are part of the Assets as described therein, true and correct copies of which have been or will be delivered to Buyer, and to the knowledge of the Company, such Assets are otherwise generally useable in the ordinary course of business. The tangible assets of the Company that are part of the Assets are in good operating condition and repair, ordinary wear and tear excepted; provided however that this sentence shall not be deemed to apply to any of the Deposit Assets. Except for the Deposit Assets, none of the personal or movable property owned or leased by the Company is located other than at the real property leased by the Company.

(d) Equipment. All Equipment is free and clear of Liens (other than Permitted Liens).

3.8 Compliance with Laws; Permits»

. Except for violations which would not reasonably be expected to result in a material adverse effect on the Assets or the business, financial condition, results of operations or prospects of the Business, the Company is not, nor has it been in the past five (5) years, in violation of any Rules applicable to it in connection with the Assets or the operation of the Business, and the Company has received no written notice of any such violation or alleged or potential violation; provided, that to the extent the representations contained in other sections of this Agreement address compliance with specific Rules (including without limitation, representations contained in **Sections 3.9**, **3.14** and **3.23**), any representations contained in this **Section 3.8** are qualified to the extent set forth in such other sections of this Agreement. Without limiting the generality of the foregoing, the Company is and has been in material compliance with all applicable Rules affecting the use, possession, distribution, labeling, advertising and all forms of promotion in connection with the sale and distribution of the Company's products, including, without limitation, that it and its representatives have not used or made any deceptive, misleading, manipulative or intentionally or inaccurate marketing or advertising materials, statements or practices. The Company holds and at all times has held all of the material Permits necessary for the use, occupancy or operation of the Business or ownership of the Assets, all of which are set forth on Schedule 3.8. The Company is and at all times has been in full compliance with each of such Permits, all of which are in full force and effect.

3.9 Real Property; Environmental and Safety Requirements.

(a) The Company does not own any real property.

(b) To the knowledge of the Company, the Company (with regard to the Business) has complied and is in compliance with all applicable Environmental and Safety Requirements, and the Company possesses all required Permits and has filed all notices or applications, required thereby.

(c) With regard to the Business (i) the Company has never (other than safely and fully in accordance with all applicable guidelines and laws) generated, transported, treated, stored, disposed of, arranged for the disposal of or otherwise handled any Hazardous Materials at any site, location or facility owned or operated or used by the Company in the Business or at any offsite location and (ii) no Hazardous Materials are present on, in, under or emanating from the real property leased by the Company, and such property contains no Hazardous Materials except as, in the case of either clause (i) or (ii) above, would not result in a condition in violation of, or any liability under, any applicable Environmental and Safety Requirements. To the knowledge of the Company, there are no underground storage tanks on the property leased by the Company.

(d) With regard to the Business, the Company has not been subject to, nor has the Company received any notice (written or oral) of, any private, administrative or judicial action, order, or investigation or any notice (written or oral) of any intended private, administrative, or judicial action, order or investigation relating to any violation of Environmental and Safety Requirements or the presence or alleged presence of Hazardous Materials in, under, upon, or emanating from any real or immovable property now or previously owned or used by the Company in the Business or any offsite location, and, to the knowledge of the Company, there is no reasonable basis in fact or law for any such notice or action; and there are no pending or threatened actions, investigations or, to the knowledge of the Company, orders or proceedings (or notices of potential actions or proceedings) from any Governmental Authority or any Person regarding any matter relating to Environmental and Safety Requirements.

3.10 Personal Property Leases»

. The Company is not a party to any lease of personal or movable property with respect to the Assets.

3.11 Contracts»

. Schedule 3.11 is a correct and complete list of every Contract, correct and complete copies of which previously have been furnished to Buyer (except for oral contracts, written descriptions in detail of which have been previously furnished to Buyer). Each of the Assumed Contracts, along with the remainder of the MAST License that is not an Assumed Contract (collectively, the "**R&W Contracts**"), is enforceable against the Company and against any third parties in accordance with its terms. The Company is not in default, and no event has occurred which with the giving of notice or the passage of time or both would constitute a default by the Company, under any R&W Contract. The Company has performed all obligations required to be performed by it under the R&W Contracts and, to the knowledge of the Company, no other party to the R&W Contracts is in default, and no event has occurred which with the giving of notice or the passage of time or both could constitute a default by any other party to any such R&W Contract under any of such R&W Contracts. Each of the R&W Contracts is in full force and effect, is valid and enforceable in accordance with its terms, and, to the knowledge of the Company, is not subject to any claims, charges, set-offs or defenses. No R&W Contract is required to be treated as a capital lease by GAAP. Except as set forth on Schedule 3.11, all of the R&W Contracts will continue, without change or modification, in full force and effect after the consummation of the transactions contemplated by this Agreement, without the necessity of obtaining any consent, approval, novation or waiver of any third party.

3.12 Brokers' or Finders' Fees»

. No agent, broker, investment banker, Person or firm acting on behalf of the Company or any stockholder thereof, or under the authority thereof, is or will be entitled to any brokers' or finders' fee or any other commission or similar fee directly or indirectly from any of the parties hereto in connection with any of the transactions contemplated hereby.

3.13 Proprietary Rights.

(a) Except as set forth on Schedule 3.13(a), the Company owns, or is licensed, or otherwise possesses legally enforceable rights, to use, sell or license, as applicable, all Proprietary Rights used, sold or licensed in connection with the Business. Schedule 1.1(a)(iv)(a), Schedule 1.1(a)(iv)(b), Schedule 1.1(a)(ix) and Schedule 1.1(b) Excluded Assets together contain a complete and correct list of all of the Company's patents and patent applications; trademark and service mark registrations and applications for registration thereof; domain names; copyright registrations and applications for registration thereof; and material computer software, in each case owned or used by the Company and primarily related to the Business (excluding Commercial Software in each case (as defined below)). The Company has delivered or shall deliver to Buyer correct and complete copies of all such patents, registrations and applications and has made available to Buyer correct and complete copies of all written documentation evidencing ownership and prosecution (if applicable) of each such item. All renewal and maintenance fees in respect of the items listed in Schedule 1.1(a)(iv)(a), Schedule 1.1(a)(iv)(b) and Schedule 1.1(a)(ix) (if applicable) have been duly paid.

(b) Schedule 3.13(b) sets forth a compete list of all (excluding Commercial Software) licenses, sublicenses and other agreements as to which the Company is a party (as licensor, licensee or otherwise) and pursuant to which the Company or any other Person is authorized to use, sell, distribute or license any Proprietary Rights in connection with the Business. The Company has delivered to Buyer correct and complete copies of all such licenses, sublicenses and agreements (as amended to date). The Company is not in violation, in any material respect, of any such license, sublicense or agreement and such license, sublicense and agreement will continue to be legal, valid, binding, enforceable and in full force and effect following the Closing.

(c) Except as disclosed on Schedule 1.1(a)(iv)(a) and Schedule 1.1(a)(iv)(b), the Company is the sole and exclusive owner of the Proprietary Rights (free and clear of any Liens) identified on such Schedules. The Company is not contractually obligated to pay compensation to any third party with respect to any Proprietary Rights, except pursuant to the agreements disclosed on Schedule 3.13(b). Each item of Proprietary Rights identified on Schedules 1.1(a)(iv)(a), 1.1(a)(iv)(b) and 1.1(a)(ix) will, immediately subsequent to the Closing hereunder, be owned or available for use by Buyer on such terms as are substantially identical to those pursuant to which the Company, immediately prior to the Closing, owns or has the right to use such item. Immediately following the Closing, the Company shall make available to Buyer all correspondence and memoranda between the Company and its intellectual property counsel relating to Proprietary Rights.

(d) To the knowledge of the Company, it has not infringed on, misappropriated or violated any proprietary rights of any third Persons in connection with the Business.

(e) No claims with respect to the Proprietary Rights used, sold or licensed in connection with the Business are pending or, to the knowledge of the Company, threatened by any Person, (i) alleging that the manufacture, sale, licensing or use of any such Proprietary Rights as now manufactured, sold, licensed or used by the Company in the Business infringes on any intellectual property rights of any third party, (ii) against the use by the Company of any technology, know-how or computer software used in the Business as currently conducted or (iii) challenging the ownership by the Company or the validity of any Proprietary Rights identified on Schedule 1.1(a)(iv)(a) and Schedule 1.1(a)(iv)(b).

(f) The Company has taken all reasonable measures to safeguard and maintain its property rights in all Proprietary Rights owned by the Company in connection with the Business. The Company is not aware of any grounds to assert a claim to, or any ownership interest in, any Proprietary Right as a result of having been involved in the development of such property while employed by or consulting to the Company. All of the computer software products within the Proprietary Rights owned by the Company in connection with the Business that have been developed by employees of the Company within the scope of their employment as a "work made for hire", which employees were directed by the Company to work on the software for which Proprietary Rights are owned by the Company, or by consultants who have assigned all rights to such products to the Company.

(g) The Company has licenses for all Commercial Software used in the Business and the use of such Commercial Software has been in accordance with such licenses. "**Commercial Software**" means packaged commercially available software programs generally available to the public.

3.14 Employee Benefit Plans.

(a) No Employee Benefit Plan is (i) subject to Section 302 or Title IV of the Employee Retirement Income Security Act of 1974, as amended ("**ERISA**") or Section 412 of the Code, (ii) a "multi-employer plan" (as such term is defined in Section 3(37) of ERISA), or (iii) a "multiple employer welfare arrangement" (as defined in Section 3(40) of ERISA).

(b) Each Employee Benefit Plan and all related trusts, insurance contracts and funds have been maintained, funded and administered in compliance with their terms and the terms of any applicable collective bargaining agreement, and in compliance with the applicable provisions of ERISA, the Code, and any other applicable legal requirement. With respect to each Employee Benefit Plan, all required payments, premiums, contributions, distributions or reimbursements for all periods ending prior to or as of the date hereof have been made or properly accrued on the Company's relevant balance sheets and financial statements.

(c) The Company does not have any liability (or potential liability) with respect to any "employee benefit plan" (as defined in Section 3(3) of ERISA) by reason of being treated as a single employer under Section 414 of the Code or Section 4001(b) of ERISA with any trade, business or entity other than the Company. The transactions contemplated by this Agreement are not transactions to evade or avoid liability (as described in Section 4069(a) or 4212(c) of ERISA).

(d) Each Employee Benefit Plan that is subject to the health care continuation requirements of Part 6 of Subtitle B of Title I of ERISA and Section 4980B of the Code (collectively, "**COBRA**") has been administered in compliance with such requirements.

3.15 Labor and Employment Matters»

. The Company is not party to or bound by any collective bargaining agreement in connection with the Business; (ii) no labor organization or group of employees has filed any representation petition or made any written demand for recognition in connection with the Business; (iii) no organizing or decertification efforts are underway or, to the knowledge of the Company, threatened in connection with the Business; (iv) since January 1, 2000, no labor strike, work stoppage, slowdown, or other material labor dispute has occurred in connection with the Business, and none is underway or, to the knowledge of the Company, threatened; and (v) there is no employment-related charge (including, but not limited to, an unfair labor practice charge), complaint, grievance, investigation, inquiry or obligation of any kind in connection with the Business, pending or, to the knowledge of the Company, threatened, in any forum, relating to an alleged violation or breach by the Company (or its officers or directors) of any law, regulation or contract.

3.16 Suppliers»

. Schedule 3.16 is a complete and correct list by dollar volume of the ten (10) largest suppliers to the Company (in terms of the Company's purchases from such suppliers during the relevant periods) of key materials and services and commodities, exclusive of utility services, with respect to the Business for each of the three most recent calendar years (each, a "**Supplier**"). Except as set forth on Schedule 3.16, (i) all Suppliers continue to be suppliers of the Business, and (ii) the Company is not involved in any material claim, dispute or controversy with any Supplier. To the Company's knowledge, since December 31, 2006, there has been no material adverse change in the relationship between the Company and any Supplier.

3.17 Customers»

. Schedule 3.17 is a complete list by dollar volume of sales made or services provided by the Company to the customers of the Business (the "**Customers**") for each of the three most recent calendar years, along with the aggregate revenue received by the Company from each Customer during each such period. Except as set forth on Schedule 3.17 and as contemplated by the Medtronic Assignment and the Transaction Documents, (i) all Customers continue to be customers of the Business, (ii) since December 31, 2006, no Customer has modified or, to the Company's knowledge, indicated that it intends to modify its relationship with the Business in a manner that is materially less favorable to the Business than the terms and conditions provided to the Business on such date, and (iii) the Company is not involved in any material claim, dispute or controversy with any Customer. Except as contemplated by the Medtronic Assignment and the Transaction Documents, no Customer has threatened to take any of the actions described in this **Section 3.17** as a result of the transactions contemplated by this Agreement. To the Company's knowledge, since December 31, 2006, there has been no other material adverse change in the relationship between the Company and any Customer.

3.18 Distributors and Representatives»

. Schedule 3.18 is a complete list of all distributors, representatives and agents for the sale of the products of the Business made during the most recent calendar year and all distributors, representatives and agents to whom the Company has given any exclusive rights with respect to territories or products in connection with the Business, indicating in each case the existing contractual arrangements, if any, with such distributor, representative or agent.

3.19 Affiliate Transactions»

. Schedule 3.19 sets forth the parties to and the date, nature and amount of each transaction (other than the provision of service as an employee or director, and compensation therefore) involving the transfer of any cash, property or rights to or from the Company from, to or for the direct or indirect benefit of any Affiliate or former Affiliate of the Company ("**Affiliate Transactions**") with respect to the Business since January 1, 2005. Except as set forth on Schedule 3.19, no officer, director, employee, or Affiliate or any entity in which any such Person or individual is an officer, director or the owner of fifteen percent (15%) or more of the beneficial ownership interests, is a party to any agreement, contract, commitment or transaction with the Company in connection with the Business (other than the provision of service as an employee or director, and compensation therefore) or has any interests in any property used by the Company in connection with the Business. Each Affiliate Transaction was effected on terms equivalent to those which would have been established in an arms-length negotiation, except as disclosed on Schedule 3.19. Except as set forth in Schedule 3.19, neither the Company nor any of its Affiliates has any direct or indirect interest in any competitor of the Business.

3.20 Insurance Policies»

. Schedule 3.20 contains a correct and complete list and description (including policy numbers, carriers, risks insured, amounts of coverage, deductibles and expiration dates) of all insurance policies currently owned by the Company pertaining to the Business or the Assets, which policies are in full force and effect, and the Company is not in default under any of them. The Company has received no written notice of cancellation or intent to cancel or increase premiums with respect to such policies nor, to the knowledge of the Company, is there any basis for any such action. None of such policies will terminate, lapse or be modified (with or without the giving of notice or lapse of time) by reason of the transactions contemplated by this Agreement. Schedule 3.20 also contains a list of all pending claims filed by the Company with any insurance company and any instances within the previous three (3) years of a denial of coverage of the Company by any insurance company, in each case in connection with the Business.

3.21 Taxes.

(a) The Company has filed all Tax Returns that it is required to have filed prior to the date hereof, including any extension of time for the filing thereof, and such returns are true and correct in all material respects and have been prepared in a manner consistent with prior periods.

(b) There are no security interests on any of the Assets that arose in connection with any failure (or alleged failure) to pay any Tax.

(c) There are no agreements, waivers or other arrangements providing for extension of filing with respect to any Tax Return. There are no unexpired waivers of any statute of limitations with respect to any Taxes.

(d) No claim has ever been made by an authority in a jurisdiction where the Company does not file Tax Returns that it is or may be subject to taxation by that jurisdiction in connection with the Business.

(e) The Company has timely withheld and paid all Taxes required to have been withheld and paid in connection with any amounts paid or owing to any employee, independent contractor, stockholder, or other third party in connection with the Business, and all Forms W-2 and 1099 required with respect thereto have been properly completed and timely filed.

(f) The Company is not a party to any action or proceedings by any Governmental Authority for the collection or assessment of Taxes.

(g) There is no dispute or claim concerning any Tax liability of the Company either (i) claimed or raised by any authority in writing or (ii) as to which any of the directors and officers (and employees responsible for Tax matters) of the Company has knowledge based upon personal contact with any agent of such authority.

(h) The Company has not made any payments, is not obligated to make any payments, nor is a party to any agreement that under certain circumstances could obligate it to make any payments that will not be deductible under Code §280G. The Company is not a party to any Tax allocation or sharing agreement (other than this Agreement, if applicable). The Company has no liability for the Taxes of any Person under Regulation §1.1502-6 (or any similar provision of state, local, or foreign law), as a transferee or successor, by contract, or otherwise. The Company has not been a United States real property holding corporation within the meaning of Code §897(c)(2) during the applicable period specified in Code §897(c)(1)(A)(ii).

(i) The Company has not made any change in any method of accounting which could give rise to the recognition of income or to Tax liability to Buyer following the date hereof. The Company has not made any closing adjustment in connection with an audit which could give rise to the recognition of income or to Tax liability to Buyer following the date hereof. The Company has not entered into any installment sale transaction (aside from this Agreement, if applicable) which could give rise to the recognition of income or to Tax liability to Buyer following the date hereof.

3.22 Litigation»

. Except as set forth on Schedule 3.22, there are no claims, counter-claims, actions, suits, grievances, arbitrations, orders, proceedings or, to the knowledge of the Company, investigations pending or, to the knowledge of the Company, threatened, against or involving the Company with respect to the Business (or pending or, to the knowledge of the Company, threatened against any of the officers, directors or key employees of the Company with respect to their business activities on behalf of the Company with respect to the Business), the Assets, or relating to the transactions contemplated hereby, before any court, agency, arbitrator or other Governmental Authority; nor, to the knowledge of the Company, is there any reasonable basis for any such claim, action, suit, proceeding or governmental investigation. Except as set forth in Schedule 3.22, the Company is not directly subject to or affected by any order, judgment, decree or ruling of, or settlement enforceable in, any court or Governmental Authority in connection with the Business. Except as set forth on Schedule 3.22, the Company is not engaged in any legal action to recover monies due it or for damages sustained by it in connection with the Business.

3.23 Product Warranties»

. To the knowledge of the Company, all commercialized Products have been in conformance with all applicable contractual commitments and all express or implied warranties of the Company, and no Liability exists for replacement thereof, recall or other damages in connection with such sales or deliveries at any time prior to the date hereof. The Company has not been notified in writing of any claims for and, to the knowledge of the Company, there are no threatened claims for any product returns, recalls, warranty obligations or product services relating to any of its Products (including, without limitation, information products) or services in connection with the Business.

3.24 Defects in Products or Designs; Product Safety.

(a) To the knowledge of the Company, there have been no pattern of defects in the design, construction or manufacturing of any Product commercialized by the Company or its employees or agents in connection with the Business that would adversely affect the specified performance or quality of such Product. Each commercialized Product has been designed, manufactured, packaged and labeled in compliance with all regulatory, engineering, industrial and other codes applicable thereto and the Company has received no written notice of any alleged noncompliance with any such code. Each Product advertised or represented as being rated or approved by a rating organization, such as Underwriters' Laboratories or other similar organizations, complies with all conditions of such rating or approval.

(b) Other than standard information and reports provided with respect to medical device products to the FDA and any local authorities, and standard international reporting to notified bodies, and vigilance reporting, the Company has not been required to file, nor has it filed, a notification or other report with the United States Consumer Product Safety Commission or any other Governmental Authority concerning actual or potential hazards with respect to any Product.

3.25 Absence of Certain Payments»

. Neither the Company nor, to the knowledge of the Company, any manager, officer, agent, employee or other Person acting on behalf of the Company has, with respect to the Business (a) used any corporate or other funds for unlawful contributions, payments, gifts or entertainment, or made any unlawful expenditures relating to political activity to government officials or others or established or maintained any unlawful or unrecorded funds in violation of Section 104 of the Foreign Corrupt Practices Act of 1977 (15 U.S.C. §79dd-2), as amended, or any other applicable provincial, foreign, federal or state law; or (b) accepted or received any unlawful contributions, payments, expenditures or gifts or (c) established or maintained any fund or asset that has not been recorded in the books and records of the Company.

3.26 Government Contracts and Funding»

. The Company is not, with respect to the Business, party to, or bound by the provisions of, any contract (including purchase orders, blanket purchase orders and agreements and delivery orders) with the United States government or any department, agency, or instrumentality thereof or any other Governmental Authority. The Company has not, with respect to the Business received any grant or other funding from any Governmental Authority, including without limitation any such grant or funding arising from a contract which contains a grant-back provision or other encumbrance based on non-use thereof.

3.27 Regulatory Approvals and Proceedings»

. The Company has made all filings and filed all reports required to be made and filed in connection with its manufacturing of Products in the U.S. and under European Community Regulations. All such applications and submissions by the Company to Governmental Authorities, including but not limited to submissions of 510(K) notification packages and Design Dossiers under European Community Regulations, and all data collection, testing and analysis in connection therewith, have been collected in a controlled manner using methods and techniques generally accepted by the industry, and all such applications and submissions have been true, complete and accurate in all material respects.

3.28 Disclosure»

. To the Company's knowledge, this Agreement, the Company Transaction Documents, the schedules and exhibits hereto, and the financial information and other materials referred to herein as having been delivered to Buyer, do not contain any untrue statement of a material fact that has not been corrected by the Company prior to the date hereof, and do not omit to state a material fact necessary in order to make the statements contained therein or herein not misleading in light of the circumstances under which they were made. There is no fact known to the Company relating to the Business, its affairs, assets, prospects, operations, employee relations or condition, financial or otherwise, that may materially adversely affect the same which has not been disclosed in writing to Buyer by the Company.

ARTICLE IV

REPRESENTATIONS AND WARRANTIES OF BUYER

Buyer hereby represents and warrants to the Company as follows:

4.1 Organization and Good Standing»

. Buyer is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware.

4.2 Authorization»

. Buyer has full power, right and authority to enter into and perform its obligations under this Agreement and each of the Buyer Transaction Documents. The execution, delivery and performance of this Agreement and each of the Buyer Transaction Documents and the consummation of the transactions contemplated hereby have been duly and validly authorized by all requisite action in accordance with applicable Rules, and no other proceedings are necessary to authorize the execution, delivery and performance of this Agreement and each of the Buyer Transaction Documents. This Agreement and each of the Buyer Transaction Documents have been duly executed and delivered by the Buyer and constitute the valid and binding obligations of the Buyer and are enforceable against the Buyer in accordance with their respective terms, except as may be limited by bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium or other laws of general application relating to the enforcement of creditors' rights and general equitable principles (whether considered in a proceeding in equity or at law).

4.3 No Violation»

. The execution, delivery and performance by Buyer of this Agreement and the other Buyer Transaction Documents and the consummation of the transactions contemplated herein and therein will not:

(a) result in the breach of any of the terms or conditions of, or constitute a default under, or in any manner release any party thereto from any obligation under, any mortgage, note, bond, contract, indenture, agreement, license or other instrument or obligation of any kind or nature to which Buyer is now a party or by which any of its properties or assets may be bound;

(b) violate any order, writ, injunction, regulation, statute or decree of any court, administrative agency or Governmental Authority specifically applicable to Buyer; or

(c) violate any provision of the governing documents of Buyer.

ARTICLE V

CLOSING

5.1 Closing»

. The transactions that are the subject of this Agreement shall be consummated at a closing (the "**Closing**") which shall be held at the offices of Katten Muchin Rosenman LLP, 525 West Monroe Street, Chicago, Illinois 60661 (or at such other place as the parties may mutually agree) on the date hereof (the "**Closing Date**"). The Closing shall be deemed effective at the close of business on the Closing Date (the "**Effective Time**").

5.2 Deliveries by the Company»

. At the Closing, the Company shall execute and deliver to Buyer:

(a) Instruments of Conveyance. The Bill of Sale, a Patent Assignment to be filed with the United States Patent and Trademark Office immediately following the Closing, an Assignment of Domain Name Registrations and any other required assignments of Proprietary Rights in form and substance satisfactory to Buyer.

(b) Opinion of Counsel. An opinion of counsel of the Company, dated as of the Closing Date, in the form reasonably requested by Buyer.

(c) Secretary's Certificate. A certificate of the Secretary of the Company certifying as to (i) resolutions of the Board of Directors of the Company authorizing the execution and delivery of this Agreement and the Company Transaction Documents and the performance of the transactions contemplated hereby and thereby; and (ii) a certificate of good standing of the Company, dated as of a date not more than fifteen (15) days prior to the Closing Date, issued by the applicable Secretary of State.

(d) Third Party Consents. Third party consents for those contracts identified on Schedule 3.4.

(e) Assignment of Medtronic Supply Agreement. An Assignment by the Company to Buyer of the Medtronic Supply Agreement (the "**Medtronic Assignment**").

(f) Transition Agreement. A Transition Services Agreement between the Company and Buyer (the "**Transition Agreement**").

5.3 Deliveries by Buyer»

. At the Closing, Buyer shall deliver to the Company:

(a) Instruments of Assumption. The Bill of Sale, executed by Buyer.

(b) Opinion of Counsel. An opinion of counsel of Buyer, dated as of the Closing Date, in the form reasonably requested by the Company.

(c) Cash Payment. The Cash Payment wired to the bank account(s) designated by the Company.

(d) Resolutions. Resolutions of Buyer authorizing the execution and delivery of this Agreement and the Buyer Transaction Documents and the performance of the transactions contemplated hereby and thereby certified by the Secretary of Buyer.

(e) Transition Agreement. The Transition Agreement executed by Buyer.

(f) Assignment of Medtronic Supply Agreement. The Medtronic Assignment executed by Buyer and Medtronic.

ARTICLE VI

COVENANTS AFTER CLOSING

6.1 Non-Assignable Contracts»

. To the extent that the assignment hereunder by the Company to Buyer of any Assumed Contract is not permitted or is not permitted without the consent of any other party to the Assumed Contract, this Agreement shall not be deemed to constitute an assignment of any such Assumed Contract if such consent is not given or if such assignment otherwise would constitute a breach of, or cause a loss of contractual benefits under, any such Assumed Contract, and Buyer shall not assume any obligations or liabilities thereunder. With respect to any such Assumed Contract, the Company shall continue to use

reasonable efforts to obtain such consents and shall cooperate with Buyer in any arrangement designed to provide Buyer with the rights and benefits (subject to the obligations) under any such Assumed Contracts.

6.2 Payment of Excluded Liabilities»

. After the Closing, the Company shall pay in full and discharge all of the Excluded Liabilities in accordance with their stated terms, as applicable, and in a manner that is not detrimental to any relationships of Buyer or the Business with customers, suppliers or others.

6.3 Agreements Regarding Tax Matters»

. After the Closing, the Company on one hand and Buyer on the other hand will (i) promptly inform the other party in writing of any notice that it receives of any audit, investigation, request for documents or information related to Taxes that could affect the Tax liability of the other party, (ii) each provide the other party with such assistance as may reasonably be requested in connection with the preparation of any Tax Return, audit or other examination by any taxing authority or judicial or administrative proceeding relating to liability for taxes, (iii) each retain and provide to the other party all records and other information that may be relevant to any such Tax Return, audit or examination, proceeding or determination and (iv) each provide the other party with any final determination of any such audit or examination, proceeding or determination that affects any amount required to be shown on any Tax Return of the other party for any period. Without limiting the generality of the foregoing, each of the Company and Buyer will retain, until the expiration of the applicable statutes of limitation (including any extensions thereof), copies of all Tax Returns, supporting work schedules and other records relating to tax periods or portions thereof ending on or prior to the Closing Date.

6.4 Indemnification.

(a) Indemnification by the Company. From and after the Closing, the Company agrees to indemnify, defend and save Buyer, its stockholder and their respective Affiliates and Plan Affiliates, and each of their respective officers, directors, employees, attorneys, agents, Employee Benefit Plans and fiduciaries, plan administrators or other parties dealing with such plans (each, a "**Buyer Indemnified Party**"), forever harmless from and against, and to promptly pay to a Buyer Indemnified Party or reimburse a Buyer Indemnified Party for, any and all liabilities, obligations, deficiencies, demands, claims, suits, actions, or causes of action, assessments, losses, costs, expenses, interest, fines, penalties, actual or punitive damages or costs or expense of any and all investigations, proceedings, judgments, environmental analysis, remediations, settlements and compromises (including reasonable fees and expenses of attorneys, accountants and other experts) (individually and collectively, the "**Losses**") sustained or incurred by any Buyer Indemnified Party relating to, resulting from, arising out of or otherwise by virtue of any of the following:

(i) any inaccuracy in or misrepresentation or breach of a representation or warranty made by the Company herein or in the Company Transaction Documents;

(ii) any non-compliance with or breach by the Company of any of the covenants or agreements contained in this Agreement or the Company Transaction Documents to be performed by the Company;

(iii) any Patent Infringement Claim or any action, demand, proceeding, investigation or claim by any third party (including Governmental Agencies) against or affecting any Buyer Indemnified Party which, if successful, would result from a matter constituting an inaccuracy in, misrepresentation or breach of any of the representations, warranties or covenants of the Company in this Agreement or any Company Transaction Documents;

(iv) any matter set forth on Schedule 3.13(e) or Schedule 3.22;

(v) any liability or obligation of the Company or any assertion against a Buyer Indemnified Party, arising out of or relating, directly or indirectly, to any of the Excluded Liabilities, including but not limited to any claim made in connection with the Products (whether or not such claims are described in **Section 6.8**);

(vi) any claim for payment of fees and/or expenses as a broker or finder in connection with the origin, negotiation, execution or consummation of this Agreement based upon an alleged agreement between claimant and the Company or any of its Affiliates; and

(vii) any non-compliance with or breach by the Company of any of the covenants or agreements contained in the MAST License to be performed by the Company.

(b) Indemnification by Buyer. From and after the Closing, Buyer agrees to indemnify, defend and save the Company, its stockholders and their respective Affiliates, and each of their respective officers, directors, employees, attorneys, agents, Employee Benefit Plans and fiduciaries, plan administrators or other parties dealing with such plans (each, a "**Company Indemnified Party**") forever harmless from and against, and to promptly pay to a Company Indemnified Party or reimburse a Company Indemnified Party for, any and all Losses sustained or incurred by any Company Indemnified Party relating to, resulting from, arising out of or otherwise by virtue of any of the following:

(i) any inaccuracy in or misrepresentation or breach of a representation or warranty made by Buyer herein or in the Buyer Transaction Documents;

(ii) non-compliance with or breach by Buyer of any of the covenants or agreements contained in this Agreement or the Buyer Transaction Documents to be performed by Buyer;

(iii) any action, demand, proceeding, investigation or claim by any third party (including Governmental Agencies) against or affecting any Company Indemnified Party which, if successful, would result from a matter constituting an inaccuracy in, misrepresentation or breach

of any of the representations, warranties or covenants of Buyer in this Agreement or any Buyer Transaction Documents;

(iv) any liability or obligation of Buyer or any assertion against a Company Indemnified Party, arising out of or relating, directly or indirectly, to any of the Assumed Liabilities and/or the Buyer's operation of the Business or usage of the Assets after the Closing Date, except to the extent such Loss arises out of the operation of the Business or ownership of the Assets prior to the Closing or is otherwise an indemnifiable Loss pursuant to **Section 6.4(a)**; and

(v) any non-compliance with or breach by Buyer of any of the covenants or agreements contained in Buyer's Assumed MAST License to be performed by Buyer.

(c) Indemnification Procedure for Third Party Claims. In the event that subsequent to the Closing any Person entitled to indemnification under this Agreement (an "**Indemnified Party**") receives notice of the assertion of any claim or of the commencement of any action or proceeding by any Person who is not a party to this Agreement or an Affiliate of a party to this Agreement, including without limitation, a Patent Infringement Claim, (a "**Third Party Claim**") against such Indemnified Party, against which a party to this Agreement is required to provide indemnification under this Agreement (an "**Indemnifying Party**"), the Indemnified Party shall give written notice together with a statement of any available information regarding such claim (and attaching a copy of all papers served with respect to such claim) to the Indemnifying Party within fifteen (15) days after learning of such claim (or within such shorter time as may be necessary to give the Indemnifying Party a reasonable opportunity to respond to such claim) (the "**Claim Notice**"). The Indemnifying Party will have the right to defend the Indemnified Party against the Third Party Claim with counsel of the Indemnifying Party's choice, satisfactory to Indemnified Party, so long as (A) the Indemnifying Party notifies the Indemnified Party in writing within thirty (30) calendar days after receipt of a Claim Notice (the "**Control Notice**") that the Indemnifying Party will undertake to assume the defense of such Third Party Claim and will indemnify the Indemnified Party against such Third Party Claim, (B) the Indemnifying Party provides the Indemnified Party with evidence reasonably acceptable to the Indemnified Party that the Indemnifying Party has and will at all times continue to have the financial resources to defend against the Third Party Claim and fulfill its indemnification obligations hereunder with respect thereto, (C) the Indemnifying Party conducts the defense of the Third Party Claim actively and diligently at its own cost and expense and (D) the Third Party Claim has not been initiated by any Governmental Authority. So long as such conditions are and remain satisfied, then the Indemnifying Party may conduct the defense of the Third Party Claim and the Indemnified Party may participate through counsel chosen by such Indemnified Party and paid at its own expense (which expense shall not constitute part of any Loss that is the subject of indemnity under this **Section 6.4** unless the Indemnified Party has reasonably concluded that counsel chosen by the Indemnifying Party has actual or potential conflicts of interest and has so notified the Indemnifying Party in writing). If the Indemnifying Party does not deliver a Control Notice within the thirty (30) day period provided above or any of the conditions set forth in clauses (A) through (D) above are or become unsatisfied, the Indemnified Party shall have the right to undertake the settlement or defense of the claim, but shall not thereby waive any right to indemnity from the Indemnifying Party therefor. The Person handling such defense or settlement shall pursue such defense or settlement with the customary care that a reasonably prudent person would exercise under the circumstances. If the Indemnifying Party decides not to undertake the conduct and control of the settlement or defense of a claim, the Indemnified Party may undertake control of the settlement or defense of the Third Party Claim to the entire exclusion of the Indemnifying Party. The Indemnifying Party will not pay or enter into any settlement of any Third Party Claim or consent to the entry of any judgment with respect to any Third Party Claim without the prior written consent of the Indemnified Party, which consent shall not be unreasonably withheld or delayed. Furthermore, the Indemnifying Party will not consent to the entry of any judgment with respect to the matter, or enter into any settlement which either imposes an injunction or other equitable relief upon the Indemnified Party or does not include a provision whereby the plaintiff or claimant in the matter releases the Indemnified Party from all liability with respect thereto. Any final judgment entered or settlement agreed upon in the manner provided herein shall be binding upon the Indemnifying Party, and shall conclusively be deemed to be an obligation with respect to which the Indemnified Party is entitled to prompt indemnification hereunder.

(d) Direct Claims. It is the intent of the parties hereto that all direct claims by an Indemnified Party against a party hereto not arising out of Third Party Claims or related to Patent Infringement Claims shall be subject to and benefit from the terms of this **Section 6.4**. Any claim under this **Section 6.4** by an Indemnified Party for indemnification other than indemnification against a Third Party Claim or in connection with a Patent Infringement Claim (a "**Direct Claim**") will be asserted by giving the Indemnifying Party reasonably prompt written notice thereof, and the Indemnifying Party will have a period of thirty (30) calendar days within which to satisfy such Direct Claims. If the Indemnifying Party disputes the Direct Claim asserted by the Indemnified Party or fails to respond within such thirty (30) calendar day period, such dispute shall be resolved in accordance with the provisions of **Section 7.8(b)** hereof and the Indemnified Party may if it so chooses proceed directly to the mediation stage.

(e) Failure to Give Timely Notice. A failure by an Indemnified Party to give timely, complete or accurate notice as provided in **Section 6.4(c)** will not affect the rights or obligations of any party hereunder except and only to the extent that, as a result of such failure, any party entitled to receive such notice was deprived of its right to recover any payment under its applicable insurance coverage or was otherwise damaged as a result of such failure to give timely notice.

(f) Survival of Representations and Warranties: Time Limits on Indemnification Obligations. All of the representations and warranties set forth in this Agreement or in any of the other Transaction Documents shall survive the execution and delivery of this Agreement and the consummation of the transactions until they expire and terminate on the second anniversary of this Agreement, and, for the avoidance of doubt, neither the Company nor Buyer shall be entitled to recovery under such representations and warranties other than pursuant to this **Section 6.4**. If written notice of a claim has been given prior to the end of such applicable period, the termination date with regard to such claim shall be extended until such claim is fully resolved and the appropriate indemnification has been tendered.

(g) Adjustment to Purchase Price. Any indemnification received under this **Section 6.4** shall be treated by Buyer, the Company and their respective Affiliates, to the extent permitted by applicable Rules, as an adjustment to the Purchase Price unless a Final Determination causes any such amount not to constitute an adjustment to the Purchase Price for Federal tax purposes. The term "**Final Determination**" shall mean (i) any final determination of liability in respect of a Tax that, under applicable Rules, is not subject to further appeal, review or modification through proceedings or otherwise (including the expiration of a statute of limitations or a period for the filing of claims for refunds, amended returns or appeals from adverse determinations) or (ii) the payment of Tax by Buyer or the Company, whichever is responsible for payment of such Tax under applicable Rules, with respect to any item disallowed or adjusted by a taxing authority, provided that such responsible party or parties determine(s) that no action should be taken to recoup such payment and the other party agrees in writing.

(h) Indemnification Limits. The foregoing provisions of this **Section 6.4** notwithstanding:

(i) the Company shall not be liable under the indemnification obligations set forth in **Section 6.4(a)(i)** of this Agreement until, and then only to the extent that, the aggregate amount of such indemnification obligation of the Company exceeds $50,000 (the "**Basket Amount**");

(ii) the aggregate indemnification obligation of the Company pursuant to **Section 6.4(a)(i)** shall not be greater than $3,000,000 (the "**Indemnification Cap**"); and

(iii) the aggregate indemnification obligations of Buyer pursuant to **Section 6.4(b)(i)** of this Agreement shall not be greater than the Indemnification Cap.

(i) Special Rule for Fraud. Notwithstanding anything in **Section 6.4(h)** to the contrary, in the event of any breach of a representation or warranty by any party hereto that is intentional or constitutes fraud, (a) the representation or warranty that has been breached will survive the execution and delivery of this Agreement and the consummation of the transactions contemplated hereby and will continue in full force and effect for the period of the applicable statute of limitations, and (b) the limitations set forth in **Section 6.4(h)** shall not apply to any Losses that any Buyer Indemnified Party or Company Indemnified Party, respectively, may suffer, sustain or become subject to, as a result of, arising out of, relating to, or in connection with, any such breach.

(j) Investigation. The representations and warranties of the Company shall not be affected or deemed waived by reason of any investigation made by or on behalf of Buyer or by reason of the fact that Buyer should have known (as opposed to "actually knew") any such representation or warranty might be inaccurate.

(k) Right of Set-off. To the extent that any Indemnifying Party fails to satisfy an indemnification obligation pursuant to this **Section 6.4** when due in accordance with the terms hereof, the Indemnified Party may in its sole discretion set off the amount of such indemnification obligation against any amounts due and payable by the Indemnified Party to the Indemnifying Party.

6.5 Restrictive Covenants.

(a) Company's Acknowledgment. The Company agrees and acknowledges that it is necessary that the Company undertake not to utilize its special knowledge of the Business and its relationships with customers and suppliers of the Company to compete with Buyer and the Business.

(b) Non-Compete. The Company hereby agrees that for a period commencing on the Closing Date and ending five (5) years from the Closing Date (the "**Restricted Period**"), the Company will not, directly or indirectly, as agent, consultant, manager, partner or in any other capacity, operate, manage, control, engage in, participate in , or act as a consultant or advisor to, or render services (alone or in association with any Person), that provide specific Business assistance to any Person that engages in or owns, invests in, operates, manages or controls any venture or enterprise that directly or indirectly engages or proposes to engage in the Business anywhere in the world (excluding Japan) (the "**Territory**"). Notwithstanding this or any other provision of **Section 6.5**, the covenants contained herein shall not restrict the Company from developing, partnering with and/or selling regenerative cell technology to any party irrespective of whether such other party is involved with the Business, or whether or not such other party might utilize regenerative cell products in connection with the Business, or restrict the Company from any activities in so far as they relate to the SurgiWrap thin film biomaterials products of the Company.

(c) Non-Solicitation. Without limiting the generality of the provisions of **Section 6.5(b)** above, the Company hereby agrees that during the Restricted Period it will not, directly or indirectly, solicit, or participate as agent, consultant, stockholder, manager, partner or in any other capacity in any business which solicits, business from any Person which is or was a customer or supplier of the Business during the three (3)-year period preceding the date of such solicitation, or from any successor in interest to any such Person for the purpose of securing business or contracts related to the Business other than in connection with the Company's regenerative cell technology.

(d) Confidential Information. During the term of this Agreement and thereafter, the Company shall keep secret and retain in strictest confidence, and shall not, without the prior written consent of Buyer, furnish, make available or disclose to any third party or use for the benefit of the Company or any third party, any Confidential Information. As used in this **Section 6.5(d)**, "**Confidential Information**" shall mean any information relating to the business or affairs of Buyer or that is exclusively used by Company in connection with the Business immediately prior to the Closing Date, and information relating to the Business financial statements, customer identities, potential customers, employees, suppliers, servicing methods, equipment, programs, strategies and information, analyses, profit margins or other proprietary information used by the Company or the Buyer in connection with the Business; provided, however, that Confidential Information shall not include any information which is in the public domain or enters the public domain through no wrongful act on the part of the Company, and Company may make any disclosures of such Confidential Information as required by law provided reasonable advance notice is provided to Buyer to seek protective orders with respect to such disclosures.

(e) Blue-Pencil. If any court of competent jurisdiction shall at any time deem the term of any particular restrictive covenant contained in this **Section 6.5** too lengthy or the Territory too extensive, the other provisions of this **Section 6.5** shall nevertheless stand, the Restricted Period shall be deemed to be the longest period permissible by law under the circumstances and the Territory shall be deemed to comprise the largest territory permissible by law under the circumstances. The court in each case shall reduce the Restricted Period and/or Territory to permissible duration or size.

(f) Property of the Business. All memoranda, notes, lists, records and other documentation or papers (and all copies thereof), including such items stored in computer memories, or microfiche or by any other means, which will become Buyer's exclusive property (after the consummation of transactions contemplated by this Agreement), shall become Buyer's property and shall be delivered to Buyer promptly on the request of Buyer. Notwithstanding the foregoing, Company shall be allowed to retain such copies as necessary for legal, financial and regulatory files as necessary for the Company's ongoing general corporate and compliance responsibilities.

(g) Remedies. The Company acknowledges and agrees that the covenants set forth in this **Section 6.5** are reasonable and necessary for the protection of Buyer's business interests, that irreparable injury will result to Buyer if the Company breaches any of the terms of this **Section 6.5**, and that in the event of the Company's actual or threatened breach of any of the provisions contained in this **Section 6.5**, Buyer will have no adequate remedy at law. The

Company accordingly agrees that in the event of any actual or threatened breach by it of any of the provisions contained in this **Section 6.5**, Buyer shall be entitled to such injunctive and other equitable relief, without the necessity of showing actual monetary damages or posting of a bond, as may be deemed necessary or appropriate by a court of competent jurisdiction. Nothing contained herein shall be construed as prohibiting Buyer from pursuing any other remedies available to it for such breach or threatened breach, including the recovery of any damages which it is able to prove.

6.6 Further Assurances»

. Each of the parties hereto agrees that subsequent to the Closing Date, upon the reasonable request of the other party hereto from time to time, it shall execute and deliver, or cause to be executed and delivered, such further reasonable instruments and take such other commercially reasonable actions as may be necessary to carry out the transactions contemplated by this Agreement and the Transaction Documents or to vest, perfect or confirm ownership of the Assets in Buyer. Without limiting the generality of the foregoing, following the Closing, the Company shall cause fully executed copies of the documents required to record the transfer of the Proprietary Rights in jurisdictions located outside of the United States to be delivered to Buyer within seven (7) days of the Company's receipt thereof.

6.7 Post-Closing Access to Books and Records»

. From and after the Closing, except in connection with any Direct Claim, the Company and its accountants and other representatives will be given reasonable access upon reasonable notice to the books and records included in the Assets relating to the period prior to the Closing Date.

6.8 Reimbursement for Recalls»

. To the extent that Buyer is required to conduct a recall with respect to any Product, Buyer shall be entitled to indemnification under **Section 6.4(a)(v)** in an amount equal to Buyer's reasonable expense with respect to such recall; provided however, that such amounts shall be subject to the indemnification limitations set forth in **Section 6.4(h)** hereof.

6.9 Regulatory Consulting Services»

. From and after the Closing, the Company shall prepare for filing by Buyer a 510(k) submission to the U.S. FDA for the SurgiWrap product and provide assistance with the Buyer's preparation of an Assumption Application for its notified body through the transfer of Design Dossiers to Buyer and Buyer's notified body and other inputs to Buyer as may reasonably be requested. In addition, the Company shall cause Mr. Ken Kleinhenz to make himself available on reasonable notice during normal business hours and devote no more than 25 hours of consulting services to the performance of related regulatory consulting services as is reasonably requested by Buyer in relation to the Business, provided that Mr. Kleinhenz shall not be required to travel in connection with such services. The services provided pursuant to this section shall be provided at no cost to Buyer.

6.10 Receipt of Certain Notice»

. Following the Closing, the Company shall provide all necessary reports to the Buyer of all adverse events and complaints of which the Company has or gains knowledge, including any follow-up information necessary to evaluate such occurrences, related to any application which incorporates the Products or any products manufactured or sold by or on behalf of the Buyer. Any initial reports of such events referred to in this section should be forwarded to the Buyer as soon as reasonably practical and in no event later than twenty-four (24) hours following the notification to the Company of the event if the event involves patient death or serious patient injury, or within three (3) business days otherwise.

6.11 MAST Licensed Business Materials»

.

(a) In the event that, following the Closing, Buyer enters into a new agreement between Buyer and MAST (or an Affiliate thereof) whereby MAST grants to Buyer a license with respect to the MAST Licensed Business Materials in form and substance satisfactory to Buyer in its sole discretion ("**Buyer's Direct MAST License**"), then the parties shall attempt to cause that portion of the MAST License included in the Assets ("**Buyer's Assumed MAST License**") to be terminated simultaneously with the execution and delivery of Buyer's Direct MAST License.

(b) Except as otherwise contemplated by **Section 6.11(a)**, (i) the Company agrees to use its reasonable best efforts to keep the entire MAST License in full force and effect following the date hereof and (ii) the Company shall not cause or allow all or any portion of the MAST License to be amended, revoked, altered or waived in any way without the prior written consent of Buyer.

(c) Except as otherwise contemplated by **Section 6.11(a)**, (i) Buyer agrees to use its reasonable best efforts to keep Buyer's Assumed MAST License in full force and effect following the date hereof and (ii) Buyer shall not cause or allow all or any portion of Buyer's Assumed MAST License to be amended, revoked, altered or waived in any way without the prior written consent of the Company.

6.12 License from the Company»

. From and after the Effective Time, the Company hereby grants to Buyer a worldwide (except Japan), fully paid-up, royalty-free license to: (a) sell or dispose of any Asset that is marked or identified with the trade or corporate name "MacroPore" or "MacroPore Biosurgery" or any derivation thereof and (b) use the trademark "MacroPore" in connection with the products of the Business, which use shall include but not be limited to, the distribution, marking and identification of products manufactured, packaged or labeled (whether before, on or following the date hereof) with such trademark, provided that such use is not in the Craniofacial Field. The licenses hereby granted shall be irrevocable and shall survive for so long as the Medtronic Supply Agreement (as amended and restated on the date hereof, and as may be further amended or modified in the future) shall remain in effect. Prior to abandoning the trademark, Company shall first offer the trademark to the end seller under the Medtronic Supply Agreement identified above, and if they decline to accept, then to the Buyer.

ARTICLE VII

MISCELLANEOUS

7.1 Notices, Consents, etc»

. Any notices, consents or other communication required to be sent or given hereunder by any of the parties shall in every case be in writing and shall be deemed properly served if (a) delivered personally, (b) sent by registered or certified mail, in all such cases with first class postage prepaid, return receipt requested, (c) delivered by a recognized overnight courier service, or (d) sent by facsimile transmission with a confirmation copy sent by overnight courier, in each case, to the parties at the addresses as set forth below or at such other addresses as may be furnished in writing.

If to Buyer:

MacroPore Acquisition Sub, Inc.

c/o Kensey Nash Corporation

735 Pennsylvania Drive

Exton, Pennsylvania 19341

Fax No.: (484) 713-2901

Attention: Joseph W. Kaufmann

with a copy (which shall not constitute notice) to:

Katten Muchin Rosenman LLP

525 West Monroe Street

Chicago, Illinois 60661-3693

Fax No.: (312) 902-1061

Attention: David R. Shevitz, Esq.

Kimberly T. Smith, Esq.

If to the Company:

Cytori Therapeutics, Inc.

3020 Callan Road

San Diego, California 92121

Fax No.: (858) 458-0994

Attention: Christopher J. Calhoun

with a copy (which shall not constitute notice) to:

Cytori Therapeutics, Inc.

3020 Callan Road

San Diego, California 92121

Fax No.: (858) 450-4335

Attention: Jonathan Soneff

Richa Nand

Date of service of such notice shall be (w) the date such notice is personally delivered, (x) three (3) days after the date of mailing if sent by certified or registered mail, (y) one (1) day after date of delivery to the overnight courier if sent by overnight courier or (z) the next succeeding business day after transmission by facsimile.

7.2 Public Announcements»

. Neither Party shall make any public announcement or filing with respect to the transactions provided for herein without the prior consent of the other Party (not to be unreasonably withheld or delayed), except as required by law in the opinion of its counsel. Any press release or other announcement or notice regarding the transactions contemplated by this Agreement made by Buyer or the Company shall be subject to prior review by and the consent of the other Party, not to be unreasonably withheld or delayed.

7.3 Severability»

. The unenforceability or invalidity of any provision of this Agreement shall not affect the enforceability or validity of any other provision.

7.4 Amendment and Waiver»

. This Agreement may be amended, or any provision of this Agreement may be waived, provided, that, any such amendment or waiver will be binding on Buyer only if such amendment or waiver is set forth in a writing executed by Buyer, and provided, that, any such amendment or waiver will be binding upon the Company only if such amendment or waiver is set forth in a writing executed by the Company. The waiver by any party hereto of a breach of any provision of this Agreement shall not operate or be construed as a waiver of any other breach.

7.5 Counterparts»

. This Agreement may be executed simultaneously in two or more counterparts, each of which shall be deemed an original but all of which together shall constitute one and the same agreement and shall become effective when one or more counterparts have been signed by each of the parties hereto and delivered to the other. This Agreement, the Transaction Documents and each other agreement or instrument entered into in connection herewith or therewith or contemplated hereby or thereby, and any amendments hereto or thereto, to the extent signed and delivered by means of a facsimile machine or other electronic transmission, shall be treated in all manner and respects and for all purposes as an original agreement or instrument and shall be considered to have the same binding legal effect as if it were the original signed version thereof delivered in person. At the request of any party hereto or to any such agreement or instrument, each other party hereto or thereto shall re-execute original forms thereof and deliver them to all other parties, except that the failure of any party to comply with such a request shall not render this Agreement invalid or unenforceable. No party hereto or to any such agreement or instrument shall raise the use of a facsimile machine or other electronic transmission to deliver a signature or the fact that any signature or agreement or instrument was transmitted or communicated through the use of a facsimile machine or other electronic transmission as a defense to the formation or enforceability of a contract and each such party forever waives any such defense.

7.6 Expenses»

. Each of the parties shall pay all costs and expenses incurred or to be incurred by it in negotiating and preparing this Agreement and in closing and carrying out the transactions contemplated by this Agreement. Any Transfer Taxes incurred shall be split evenly between the Company and Buyer, provided that Company’s obligation for such taxes shall not exceed Thirty Five Thousand Seven Hundred Dollars ($35,700).

7.7 Headings»

. The subject headings of Articles and Sections of this Agreement are included for purposes of convenience only and shall not affect the construction or interpretation of any of its provisions.

7.8 Governing Law; Arbitration.

(a) This Agreement shall be construed and governed in accordance with the internal laws of the State of Delaware without regard to the principles of conflicting laws.

(b) The parties shall negotiate in good faith to resolve any controversy, dispute or disagreement arising out of or relating to this Agreement or the breach of any provision of this Agreement. Except as otherwise set forth in **Section 2.2**, any matter not resolved by negotiation shall be settled (a) first, by

the parties trying in good faith to settle the dispute by mediation under the Commercial Mediation Rules of the American Arbitration Association ("**AAA**") (such mediation session to be held in Chicago, Illinois and to commence within thirty (30) days of the appointment of the mediator by the AAA), and (b) if the controversy, claim or dispute cannot be settled by mediation, then by arbitration administered by the AAA under its Commercial Arbitration Rules (such arbitration to be held in Chicago, Illinois before a single neutral arbitrator selected by AAA and to commence within thirty (30) days of the appointment of the arbitrator by the AAA or such later date as is reasonable under the circumstances), and judgment on the award rendered by the arbitrator may be entered in any court having jurisdiction thereof. Nothing in this **Section 7.8(b)** shall be construed to prevent either party from seeking interim equitable relief through a court of law for violations of this Agreement.

7.9 Assignment»

. This Agreement will be binding upon and inure to the benefit of the parties hereto and their respective successors and permitted assigns, but will not be assignable or delegable by any party without the prior written consent of the other party, provided, however, that (1) Buyer shall be allowed to assign its rights and benefits hereto (a) to an Affiliate so long as the Affiliate assumes Buyer's obligations hereunder, (b) in connection with a sale of all or substantially all of Buyer's assets so long as the assignee assumes Buyer's obligations hereunder and (c) to Buyer's lenders as collateral for security purposes, and (2) the Company shall be allowed to assign its rights and benefits hereto to (a) in connection with a sale of all or substantially all of the Company's assets so long as the assignee assumes Company's obligations hereunder and the Company remains fully liable therefor and (b) to the Company's lenders as collateral for security purposes.

7.10 Definitions»

. For purposes of this Agreement, the following terms have the meaning set forth below:

"**Affiliate**" means, with respect to any Person, any other Person directly or indirectly controlling, controlled by, or under common control with such Person, and any officer, director or executive employee of such Person, and includes any past or present Affiliate of any such Person. The term "control" (including, with correlative meanings, the terms "controlling," "controlled by" and "under common control with"), as applied to any Person, includes the possession, directly or indirectly, of five percent (5%) or more of the total number of votes which may be cast by the holders of the total number of outstanding shares of stock of any class or classes of such Person in any election of directors of such Person (or in the case of a Person which is not a corporation, five percent (5%) or more of the ownership interest, beneficial or otherwise) of such Person or the power otherwise to direct or cause the direction of the management and policies of that Person, whether through voting, by contract or otherwise.

"**Affiliated Group**" means an affiliated group as defined in Section 1504 of the Code (or analogous combined, consolidated or unitary group defined under state, local or foreign income Tax law).

"**Business**" means the biomaterials polymer business (developing, manufacturing, commercializing and marketing technology and products in connection with bioresorbable polymer implants) as conducted by the Company. This term specifically excludes any and all rights to Company's thin film (SurgiWrap) polymer technology and business for the territory of Japan, and all other rights to the thin film technology owned by the Company for all other markets/applications other than for applications in the Spinal Field, and also excludes all rights to the craniomaxillofacial bioresorbable implants business which the Company sold to Medtronic in 2002.

"**Buyer Transaction Documents**" means the Bill of Sale and any other agreement, document, certificate or instrument to which the Buyer is a party and which is being delivered pursuant to this Agreement.

"**Code**" means the Internal Revenue Code of 1986, as amended.

"**Company Taxes**" means collectively (a) any Taxes imposed on the Company for any period, (b) any Taxes imposed with respect to the Assets for any period (or portion of any period) ending on or before the Effective Time and (c) Transfer Taxes in accordance with Section 7.6.

"**Company Transaction Documents**" means the Bill of Sale and any other agreement, document, certificate or instrument to which the Company is a party and which is being delivered pursuant to this Agreement.

"**Contracts**" means any contracts, commitments, purchase orders, sales orders, licenses, leases and other agreements, whether written or oral, to which the Company is a party or by which Company is bound as are necessary in connection with the conduct of the Business.

"**Craniofacial Field**" means any skeletal fixation and/or reconstruction application in each case and only to the extent that the application pertains to neurosurgery (cranial and skull base only), craniomaxillofacial, oral maxillofacial, reconstructive (head/face only), otolaryngology, orthognathic, mandibular, plastic surgery (head/face only), and/or iliac crest.

"**Deposit Agreement**" means that certain Deposit Agreement dated as of April 19, 2007 by and between the Company and Buyer.

"**Deposit Amount**" means $250,000, which amount represents the aggregate amount of the Purchase Price that has been prepaid by Buyer to the Company pursuant to the terms and conditions set forth in the Deposit Agreement.

"**Deposit Assets**" means the Assets as such term is defined in the Deposit Agreement.

"**Employee Benefit Plan**" means any "Employee Pension Benefit Plan" (as defined in Section 3(2) of ERISA), "Employee Welfare Benefit Plan" (as defined in Section 3(1) of ERISA), "Multi-Employer Plan" (as defined in Sections 3(37) or 4001(a)(3) of ERISA), pension plan, plan of deferred compensation, medical plan, life insurance plan, long-term disability plan, dental plan, "multiple employer welfare arrangement" (as defined in Section 3(40) of ERISA) or other plan or trust providing for or funding of the welfare of any of the employees or former employees or beneficiaries thereof of the Company, personnel policy (including, but not limited to, vacation time, holiday pay, bonus programs, moving expense reimbursement programs and sick leave), excess benefit plan, bonus or incentive plan (including, but not limited to, stock options, restricted stock, stock bonus and deferred bonus plans),

severance, salary reduction agreement, change-of-control agreement, employment agreement, consulting agreement or any other benefit, program or contract, whether or not written or pursuant to a collective bargaining agreement, in each case of the Company.

"**Environmental and Safety Requirements**" means all federal, state and local or municipal laws, rules, regulations, ordinances, orders, statutes and requirements, and all common law, relating to public health and safety, worker health and safety, pollution or protection of the environment, all as amended or hereafter amended.

"**GAAP**" means generally accepted accounting principles set forth in the opinions and pronouncements of the Accounting Principles Board of the American Institute of Certified Public Accountants and statements and pronouncements of the Financial Accounting Standards Board (or any successor authority) that are applicable as the date of determination, consistently applied.

"**Governmental Authority**" means any multi-national, national, state, provincial, local, governmental, judicial, public, quasi-public, administrative or self-regulatory authority, agency, commission, board, organization or instrumentality.

"**Guarantees**" means any obligation, contingent or otherwise, of the Company directly or indirectly guaranteeing any indebtedness or other obligation of any other Person. The term "guarantee" used as a verb has a corresponding meaning.

"**Hazardous Materials**" means (A) hazardous materials, hazardous substances, extremely hazardous substances or hazardous wastes, as those terms are defined by the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. §9601 *et seq.*, the Resource Conservation and Recovery Act, 42 U.S.C. §6901 *et seq.*, and any other Environmental and Safety Requirements; (B) petroleum, including, without limitation, crude oil or any fraction thereof which is liquid at standard conditions of temperature and pressure (60 degrees Fahrenheit and 14.7 pounds per square inch absolute); (C) any radioactive material, including, without limitation, any source, special nuclear, or by-product material as defined in 42 U.S.C. §2011 *et seq.*; (D) asbestos in any form or condition; and (E) any other material, substance or waste to which liability or standards of conduct may be imposed under any Environmental and Safety Requirements.

"**Indebtedness**" means without duplication, all: (a) indebtedness for borrowed money or funded debt owed by the Company, (b) Guarantees, (c) liabilities of the Company evidenced by notes, bonds or debentures, (d) liabilities of the Company secured by any Liens, (e) liabilities or obligations evidenced by a note, bond or other debt instrument, (f) the capitalized portion of lease liabilities of the Company under any capitalized lease, (g) liabilities arising from installment purchases of property or representing the deferred purchase price of property or services in respect of which the Company is liable, contingently or otherwise, as obligor or otherwise (other than trade payables and other current liabilities incurred in the ordinary course), (h) liabilities or obligations with respect to Severance Obligations, (i) all liabilities and obligations of the Company with respect to outstanding letters of credit and (j) any interest, principal, prepayment penalty, fees, or expenses, to the extent due or owing in respect of those items listed in clauses (a) through (i) above.

"**knowledge of the Company**" and each phrase having equivalent meaning (e.g., "known to the Company" or "to the Company's knowledge") means the facts or other information known by Chris Calhoun, Kevin Thomas, Tim Zander, Mark Saad, Jon Soneff, John Risley, Peter Amis, Ken Kleinhenz, Richa Nand and Eric Daniels or that would have been known by any such Person if they had made reasonable inquiry.

"**Liabilities**" means any indebtedness (including, but not limited to, any Indebtedness), obligations or liabilities of the Company of any kind or nature whatsoever, whether fixed or unfixed, absolute or contingent, accrued or unaccrued, known or unknown, liquidated or unliquidated, choate or inchoate, secured or unsecured, and whether due or to become due and regardless of when or by whom asserted, including, but not limited to, any obligations arising out of facts, circumstances or events that have occurred prior to the Closing but are not known as of the Closing but that if known would be contingent liabilities.

"**MAST**" means MAST Biosurgery AG, a Swiss corporation.

"**MAST License**" means collectively that certain (i) License Agreement dated May 13, 2004 between the Company and MAST and (ii) License Agreement dated May 23, 2006 between the Company and MAST.

"**MAST Licensed Business Materials**" means those certain items licensed by MAST pursuant to the MAST License that are necessary for the conduct of the Business, including without limitation, such items for use in the Spinal Field.

"**Medtronic**" means Medtronic, Inc., a Minnesota corporation.

"**Medtronic Supply Agreement**" means that certain Development and Supply Agreement dated as of January 5, 2000 between the Company and Medtronic, as amended by Amendment No. 1 thereto dated December 22, 2000 and Amendment No. 2 thereto dated September 30, 2002.

"**Patent Infringement Claim**" means a claim or assertion by the third party that Buyer's conduct of the Business infringes any patent owned by or licensed to such third party for which Buyer may reasonably be entitled to indemnification pursuant to **Section 6.4(a)(i), (iii)** or **(iv)**.

"**Permits**" means all permits, licenses, approvals and authorizations by or of Governmental Authorities or third parties issued or granted or otherwise received primarily in connection with the Business.

"**Permitted Liens**" means: (A) statutory liens for Taxes that are not yet due and payable; (B) statutory liens to secure obligations to landlords, lessors or renters under leases or rental agreements; and (C) deposits or pledges made in connection with, or to secure payment of, workers' compensation, unemployment insurance or similar programs mandated by applicable law.

"**Person**" means any individual, partnership, limited partnership, sole proprietorship, company or corporation with or without share capital, public or private association, public utility, legal personal representative, regulatory or Governmental Agency, or other legal entity however designated or constituted.

"**Product**" means any product of the Business manufactured or sold by the Company prior to the Effective Time.

"**Severance Obligation**" means all severance, stay bonus or change of control payment obligations of the Company and other accelerations or increases in rights or benefits of the Company's current or former employees (whether payable or occurring prior to, on or after the Closing Date), including without limitation any such obligations arising in whole or in part as a result of the consummation of the transactions contemplated by this Agreement.

"**Specified Assets**" means all Equipment and Inventory used in connection with the operation of the Business as described on Specified Assets Schedules 1.1(a) and 1.1(b).

"**Spinal Field**" means all applications (including but not limited to: anti-adhesion, anti-scarring, minimizing the attachment of soft tissues, or soft tissue support) related to the anatomy of the spine including, but not limited to, applications in the following: spinal fixation, stabilization and/or fusion, spinal cord coverings, exiting nerve root coverings, cauda equina coverings, lamina coverings and vertebral column-cervical, thoracic, lumbar and sacral. The Spinal Field does not include distal peripheral nerve and other structures extrinsic and distal to the spine.

"**Subsidiary**" means any corporation, partnership, limited liability company, association or other entity of which securities or other ownership interests representing more than fifty percent (50%) of the ordinary voting power are owned or controlled by (i) the Company, (ii) one or more Subsidiaries of the Company or (iii) the Company and one or more Subsidiaries of the Company.

"**Tax**" means any multi-national, Federal, state, local or foreign income, gross receipts, franchise, estimated, alternative minimum, add on minimum, sales, use, transfer, registration, value added, excise, natural resources, entertainment, amusement, severance, stamp, occupation, premium, windfall profit, environmental, customs, duties, real property, personal property, ad valorem, capital stock, social security, unemployment, disability, payroll, license, employee or other withholding, or other tax, of any kind whatsoever, including any interest, penalties or additions to Tax or additional amounts in respect of the foregoing; the foregoing shall include any transferee or secondary liability for a Tax and any liability assumed by agreement or arising as a result of being (or ceasing to be) a member of any Affiliated Group (or being included (or required to be included) in any Tax Return relating thereto).

"**Tax Returns**" means returns, declarations, reports, claims for refund, information returns or other documents (including any related or supporting schedules, statements or information and any amendment thereof) filed or required to be filed in connection with the determination, assessment or collection of any Taxes of any party or the administration of any laws, regulations or administrative requirements relating to any Taxes.

"**Transaction Documents**" means the Buyer Transaction Documents and the Company Transaction Documents.

"**Transfer Taxes**" means all sales, transfer, documentary, stamp, recording, conveyance and similar taxes and fees (including any penalties and interest) due with regard to the transactions contemplated by this Agreement.

7.11 Entire Agreement»

. This Agreement, the Preamble and all the Schedules and Exhibits attached to this Agreement (all of which shall be deemed incorporated in the Agreement and made a part hereof) and the Transaction Documents set forth the entire understanding of the parties, and supersede and preempt all prior oral or written understandings and agreements with respect to the subject matter hereof, and shall not be modified or affected by any offer, proposal, statement or representation, oral or written, made by or for any party in connection with the negotiation of the terms hereof, and may be modified only by instruments signed by all of the parties hereto; provided that the Deposit Agreement and any Nondisclosure/Confidentiality agreements in place between the parties are not superseded or preempted hereby.

7.12 Third Parties»

. Except as otherwise set forth in **Section 6.4**, nothing herein expressed or implied is intended or shall be construed to confer upon or give to any Person, other than the parties to this Agreement and their respective permitted successors and assigns, any rights or remedies under or by reason of this Agreement.

7.13 Interpretative Matters»

. Unless the context otherwise requires, (a) all references to Articles, Sections or Schedules are to Articles, Sections or Schedules in this Agreement, (b) each accounting term not otherwise defined in this Agreement has the meaning assigned to it in accordance with GAAP, (c) words in the singular or plural include the singular and plural, pronouns stated in either the masculine, the feminine or neuter gender shall include the masculine, feminine and neuter and (d) the term "including" shall mean by way of example and not by way of limitation. The parties hereto have participated jointly in the negotiation and drafting of this Agreement. If an ambiguity or questions of intent or interpretation arises, this Agreement shall be construed as if drafted jointly by the parties, and no presumption or burden of proof shall arise favoring any party by virtue of the authorship of any of the provisions of this Agreement.

7.14 Waiver of Bulk Sales Laws»

. Buyer and the Company hereby waive compliance in connection with the transactions contemplated by this Agreement or the Transaction Documents with the provisions of Article 6 of the Uniform Commercial Code as adopted in states where any of the Assets are located, and any other applicable bulk sales laws, in effect as of the date of the Closing; provided, however, that the Company shall fully indemnify, reimburse and hold harmless Buyer and its Affiliates against all liability, damages or expenses which Buyer may suffer due to the Company's failure to so comply.

IN WITNESS WHEREOF, the parties have executed this Agreement as of the date first above written.

THE COMPANY:

Cytori Therapeutics, Inc.,

a Delaware corporation

By: /s/ Christopher J. Calhoun

Name: Christopher J. Calhoun

Its: CEO

BUYER:

MacroPore Acquisition Sub, Inc.,
a Delaware corporation

By: /s/ Joseph W. Kaufmann

Name: Joseph W. Kaufmann

Its: President

Exhibit 10.47

CONSULTING AGREEMENT

This Consulting Agreement (this "Agreement") is entered into by and between Cytori Therapeutics, Inc., a Delaware corporation (the "Company"), and Marshall G. Cox ("Consultant"), effective as of May 3, 2007 (the "Retirement Date").

WHEREAS, Consultant is retiring and resigning from his positions as a Company director and employee, and

WHEREAS, the Company wishes to honor Consultant with recognition as Chairman Emeritus and to retain access to his advice and counsel during a transition period.

NOW, THEREFORE, in consideration of the foregoing and the mutual agreements set forth herein, the parties agree as follows.

1. Consulting Relationship. During the term of this Agreement, Consultant will provide consulting services (the "Services") on an as-needed basis to the Company as may be specified from time to time by the Company's Chief Executive Officer (the "CEO") as to scope, subject matter, timing, format and location, all in the CEO's reasonable discretion. Notwithstanding the foregoing, Consultant will not be required to travel or to perform services in the Company's offices, nor shall he be required to provide more than ten hours of service per month. Consultant generally will perform services in his own facility. When Consultant deems it necessary or appropriate to spend time in the Company's facility, the Company will provide Consultant with space to work, but Consultant will not have a regularly assigned workspace.

2. Compensation. As consideration for the Services to be provided by Consultant, the Company shall pay to Consultant $5,000 per month, payable in arrears, during the term of this Agreement. Consultant shall be responsible for all taxes on such amount. The Company shall promptly reimburse Consultant for all reasonable out-of-pocket incurred in carrying out the Services requested pursuant to this Agreement, subject to documentation in accordance with the Company's business expense reimbursement policy, as in effect from time to time. It is also understood and acknowledged that, during the term of this Agreement, and in accordance with the existing terms of the applicable stock option plans and agreements, Consultant's outstanding stock options shall continue to vest and be exercisable.

3 Term of Agreement. The term of this Agreement shall begin on the Retirement Date and end on March 1, 2009. The Company may terminate this Agreement prior to the expiration of such term only in the event that Consultant commits fraud in the commission of his Services on behalf of the Company hereunder, and has failed to cure such acts or failures to act which are alleged to constitute fraud within sixty days after receipt of written notice from the Company stating in detail the particular acts or failures to act that constitute the grounds on which the proposed termination is based.

4. Retirement. This Agreement constitutes Consultant's retirement and resignation as a Company director and employee as of the Retirement Date. This Agreement also constitutes the Company's appointment of Consultant as Chairman Emeritus for life effective upon the Retirement Date. The parties confirm that the position of Chairman Emeritus is an honorary, unpaid position and does not itself constitute Consultant an employee or consultant of the Company.

5. Independent Contractor. Consultant's relationship with the Company during the term of this Agreement will be that of an independent contractor and not that of a director, officer, employee or agent. During the term of this Agreement:

(a) No Authority to Bind Company. Consultant has no authority to enter into contracts that bind the Company or create obligations on the part of the Company, and he agrees not to purport to do so.

(b) No Benefits. Consultant acknowledges and agrees that Consultant will not, by virtue of this consultancy, be eligible for any Company employee benefits, except as provided under Sections 2, 6 and 10.

6. Other Agreements. Except as otherwise specified in this Agreement, all agreements between the Company and Consultant pertaining to his service and compensation as an employee and/or director are hereby terminated by mutual agreement and without any further obligation of either party, with the exception of Consultant's stock option agreements, any indemnification and/or insurance rights Consultant may have pursuant to the Company's certificate of incorporation, bylaws or insurance policies for officers and directors liability (provided, that the Company shall have no obligation to purchase future directors and officers liability insurance, nor renew any directors and officers liability insurance, for the purpose of covering Consultant for periods after the Retirement Date or for maintaining the benefit of coverage under past or current policies), and any employee benefit plans or agreements the provisions of which will continue to govern the Consultant's and the Company's rights and obligations with respect to benefits accrued through the Retirement Date.

7. Consulting or Other Services for Competitors. Consultant represents and warrants that Consultant does not presently perform or intend to perform, during the term of this Agreement, consulting or director or other services for, or engage in or intend to engage in an employment relationship with, companies whose businesses or proposed businesses in any way involve products or services which would be competitive with the Company's regenerative-cell products or services. If, however, Consultant decides to do so, Consultant agrees that, in advance of accepting such work, Consultant will promptly notify the Company in writing, specifying the organization with which Consultant proposes to consult, provide services, or become employed by.

8. The Employment, Confidentiality and Assignment Agreement. Consultant represents that, immediately before signing this Agreement, he has signed and delivered to the Company an Employment, Confidentiality and Assignment Agreement on the Company's standard form of such agreement, and has dated it "May 3, 2007, as of July 31, 2000" (the "Confidentiality Agreement"). The Confidentiality Agreement remains in full force and effect, and will continue to persist during the term of and after the termination or expiration of this Consulting Agreement. In addition, Consultant and the Company

mutually understand and agree that the terms of the Confidentiality Agreement shall also apply to and during the term of this Consulting Agreement, with all applicable changes to reflect and cover the fact that his service will be as a consultant rather than as an employee; provided, that this Consulting Agreement shall control in the event of any inconsistency between the provisions of the Confidentiality Agreement and this Consulting Agreement. (For example, Section 3 and the first paragraph of Section 4 of the Confidentiality Agreement shall be inapplicable during the term of consultancy.) Moreover, the Company further agrees that its remedies for any breach of the Confidentiality Agreement shall not include the right to terminate this Consulting Agreement due to such breach. Consultant confirms that his fiduciary duty as a director with regard to confidentiality of all confidential or proprietary information he learned in his capacity as a Company director persists even after his retirement and resignation from the Board of Directors and will continue to persist during the term of and after the termination or expiration of this Consulting Agreement.

9. Works Made for Hire. All works of authorship created by Consultant in connection with the Services shall be deemed "works made for hire," and shall be owned by the Company.

10. Post-Employment Matters.

(a) Salary and Vacation Time. The Company confirms its obligation to pay forthwith to Consultant all of his accrued base salary and his accrued and unused vacation/holiday/paid-time-off time through the date of this Agreement.

(b) COBRA. The Company and Consultant acknowledge that the Company has provided Consultant with forms pursuant to which he may maintain his and his eligible dependents' participation in the Company's group health insurance plan pursuant to the terms of the Consolidated Omnibus Budget Reconciliation Act and corresponding provisions of state law ("COBRA"). If Consultant elects such coverage, he understands and agrees that he shall be fully responsible for making the necessary premium payments in order to continue such coverage. Nothing herein shall limit the right of the Company to change the provider and/or the terms of its group health insurance plans or other benefit plans at any time hereafter, nor its right to terminate any or all plans at any time hereafter.

11. Dribble-Out.

(a) Limitation**.** Consultant agrees that in each of the five successive three-month periods beginning immediately after the end of the (90-day) Lock-Up Period contemplated by his Lock-Up Agreement dated February 23, 2007 given to Piper Jaffray & Co. in connection with the Company's February 2007 registered-direct offering (the "Lock-Up Agreement"), he will sell no more than 160,000 shares of Company common stock in the three-month period. These 160,000 share amounts are not cumulative, e.g., it is not the case that if he sells no shares in the first three-month period he could sell up to 320,000 shares in the second three-month period.

(b) Definition**.** This agreement not to "sell" means that Consultant agrees not to (and will cause the spouse and any immediate family member of Consultant or his spouse living in Consultant's household not to) directly or indirectly, sell (including without limitation any short sale and also including without limitation any sale pursuant to a Rule 10b5-1 stock selling plan), offer, pledge, transfer, contract or grant any option to sell, establish an open "put equivalent position" within the meaning of Rule 16a-1(h) under the Securities Exchange Act, or otherwise dispose of any shares of Common Stock, options or warrants to acquire shares of Common Stock, or securities exchangeable or exercisable for or convertible into shares of Common Stock currently or hereafter owned either of record or beneficially by Consultant (or such spouse or family member), or publicly announce an intention to do any of the foregoing, except as expressly allowed by this Section 11, during the (90-day) Lock-Up Period and also for the period commencing immediately after the end of the (90-day) Lock-Up Period contemplated by the Lock-Up Agreement and ending 15 months thereafter (the "Dribble-Out Period"). The foregoing sentence shall not apply to (i) any exercise of outstanding stock options; (ii) any transfer to the immediate family (for the purposes of this Agreement, "immediate family" shall mean any relationship by blood, marriage or adoption, no more remote than first cousin) of Consultant or to a trust the beneficiaries of which are exclusively Consultant and/or a member or members of his immediate family; or (iii) any transfer upon Consultant's death; provided, however, that in any such case of item (ii) above it shall be a condition to such transfer that the transferee executes and delivers to the Company an agreement stating that the transferee is receiving and holding the Common Stock subject to the provisions of this Section 11, and there shall be no further transfer of such Common Stock during the Dribble-Out Period except in accordance with this Agreement (with all sales by Consultant and such item (ii) transferees within the same three-month period being combined).

(c) Stop Transfer. Consultant agrees and consents to the entry of stop transfer instructions with the Company's transfer agent and registrar against the transfer of shares of Common Stock or securities convertible into or exchangeable or exercisable for Common Stock held by Consultant except in compliance with the foregoing restrictions.

(d) Securities Law Compliance. Consultant acknowledges his responsibility to ensure that any and all sales by him comply not only with this Section 11 but also with all applicable securities laws and regulations.

12. Miscellaneous.

(a) Amendments and Waiver. Any term of this Agreement maybe amended or waived only with the written consent of the parties.

(b) Sole Agreement. This Agreement constitutes the sole agreement of the parties, and (except to the extent specific other agreements are expressly provided for herein for preservation) supersedes all prior and contemporaneous negotiations, commitments and agreements, with respect to the subject matter hereof. For avoidance of doubt: the stock option and other agreements specified in Section 6, the Lock-Up Agreement dated February 23, 2007 given to Piper Jaffray & Co. in connection with the Company's February 2007 registered-direct offering and, except as specifically provided herein, the Confidentiality Agreement, are not superseded.

(c) Choice of Law. The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of California, without giving effect to the principles of conflict of laws.

(d) Arbitration. Any dispute or claim arising out of or in connection with any provision of this Agreement will be finally settled by binding arbitration in Orange County, California, in accordance with the commercial arbitration rules of the American Arbitration Association by one arbitrator appointed in accordance with said rules. The arbitrator shall apply California law, without reference to rules of conflicts of law or rules of statutory arbitration, to the substantive resolution of any dispute. Judgment on the award rendered by the arbitrator may be entered in any court having jurisdiction thereof. Notwithstanding the foregoing, the parties may apply to any court of competent jurisdiction for preliminary or interim equitable relief, or to compel arbitration in accordance with this paragraph, without breach of this arbitration provision. This Section 12(d) shall not apply to the Confidentiality Agreement.

(e) Advice of Counsel. Each party acknowledges that, in negotiating and executing this Agreement, (i) such party has had the right and the opportunity to seek the advice of independent legal counsel of his or its own choosing, (ii) such party has read and understood all of the terms and provisions of this Agreement, and (iii) Heller Ehrman LLP and Hayden Trubitt, and Jonathan Soneff, represent only the Company and did not represent and are not representing Consultant. The Company will reimburse Consultant for up to $5,000 in reasonable attorneys' fees incurred by Consultant in connection with the negotiation and preparation of this Agreement and any related agreements contemplated hereunder**.**

(f) Construction. This Agreement shall not be construed against either party by reason of who drafted or prepared it.

(g) Notices. Every notice or other communication relating to this Agreement shall be in writing, and shall be mailed to or delivered to the party for whom it is intended at such address as may from time to time be designated by it in a notice mailed or delivered to the other party as herein provided, provided that, unless and until some other address be so designated, all notices or communications by Consultant to the Company shall be mailed or delivered to the Company at its principal executive office, and all notices or communications by the Company to Consultant may be given to Consultant personally or may be mailed to Consultant at the following address:

Marshall G. Cox
[address]
[address]

with a copy to:
Jorge del Calvo and Cindy V. Schlaefer
Pillsbury Winthrop Shaw Pittman LLP
2475 Hanover Street
Palo Alto, CA 94304

Any notice so addressed shall be deemed to be given: (i) if delivered by hand, or by courier or overnight mail, on the date of such delivery; and (ii) if mailed by registered or certified mail, on the third business day after the date of such mailing.

CYTORI THERAPEUTICS, INC.

By: /s/ Marc Hedrick

Title: President

MARSHALL G. COX

/s/ Marshall G. Cox

EXHIBIT 15.1

Letter Re Unaudited Interim Financial Information

August 14, 2007

Cytori Therapeutics, Inc.
3020 Callan Rd
San Diego, California 92121

Re: Registration Statement Nos. 333-82074, 333-122691, 333-134129, and 333-140875

With respect to the subject registration statements, we acknowledge our awareness of the use therein of our report dated August 8, 2007 related to our review of interim financial information.

Pursuant to Rule 436 under the Securities Act of 1933 (the Act), such report is not considered part of a registration statement prepared or certified by an independent registered public accounting firm, or a report prepared or certified by an independent registered public accounting firm within the meaning of Sections 7 and 11 of the Act.

/s/ KPMG LLP

San Diego, California

EXHIBIT 31.1

Certification of Chief Executive Officer Pursuant to
Securities Exchange Act Rule 13a-14(a),
as Adopted Pursuant to
Section 302 of the Sarbanes-Oxley Act of 2002

I, Christopher J. Calhoun, the Chief Executive Officer of Cytori Therapeutics, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cytori Therapeutics, 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 the Exchange Act Rules 13a-15(e) and 15d-15(e)) 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) 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

(c) 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 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: August 14, 2007
/s/ Christopher J. Calhoun
Christopher J. Calhoun,
Chief Executive Officer

EXHIBIT 31.2

Certification of Chief Financial Officer Pursuant to
Securities Exchange Act Rule 13a-14(a),
as Adopted Pursuant to
Section 302 of the Sarbanes-Oxley Act of 2002

I, Mark E. Saad, the Chief Financial Officer of Cytori Therapeutics, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cytori Therapeutics, 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 the Exchange Act Rules 13a-15(e) and 15d-15(e)) 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) 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

(c) 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 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: August 14, 2007
/s/ Mark E. Saad
Mark E. Saad
Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350/ SECURITIES EXCHANGE ACT RULE 13a-14(b), AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Cytori Therapeutics, Inc. for the quarterly period ended June 30, 2007 as filed with the Securities and Exchange Commission on the date hereof, Christopher J. Calhoun, as Chief Executive Officer of Cytori Therapeutics, Inc., and Mark E. Saad, as Chief Financial Officer of Cytori Therapeutics, Inc., each hereby certifies, respectively, that:

1. The Form 10-Q report of Cytori Therapeutics, Inc. that this certification accompanies fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934.

2. The information contained in the Form 10-Q report of Cytori Therapeutics, Inc. that this certification accompanies fairly presents, in all material respects, the financial condition and results of operations of Cytori Therapeutics, Inc.

By: /s/ Christopher J. Calhoun

Dated: August 14, 2007

Christopher J. Calhoun
Chief Executive Officer

By: /s/ Mark E. Saad

Dated: August 14, 2007

Mark E. Saad
Chief Financial Officer