SONUS PHARMACEUTICALS INC

FORM 10-Q/A
(Amended Quarterly Report)

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U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON D.C. 20549

FORM 10-Q/A-1

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 1999

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM _____
TO _____.

Commission file number 0-26866

SONUS PHARMACEUTICALS, INC.

(Exact Name of Registrant as Specified in Its Charter)

DELAWARE (State or Other Jurisdiction of Incorporation or Organization)	95-4343413 (I.R.S. Employer Identification Number)

22026 20TH AVE. SE, BOTHELL, WASHINGTON 98021
(Address of Principal Executive Offices)

(425) 487-9500
(Registrant's Telephone Number, Including Area Code)

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

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date.

Class	Outstanding at October 31, 1999
Common Stock, $.001 par value	8,986,146

Exhibit Index appears on Page 14

SONUS PHARMACEUTICALS, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SONUS PHARMACEUTICALS, INC.
BALANCE SHEETS

	SEPTEMBER 30, 1999 (UNAUDITED)	DECEMBER 31, 1998
ASSETS		
Current assets:		
Cash, cash equivalents and marketable securities	$ 15,148,735	$ 16,954,842
Contract receivable	5,000,000	--
Other current assets	165,499	419,018
Total current assets	20,314,234	17,373,860
Equipment, furniture and leasehold improvements, net of accumulated depreciation of $3,061,399 and $2,552,786	974,575	1,444,090
Total assets	$ 21,288,809	$ 18,817,950
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Bank line of credit	$ 5,000,000	$ 5,000,000
Accounts payable and accrued expenses	3,974,792	2,954,530
Accrued clinical trial expenses	230,381	1,226,335
Capital lease obligations	31,022	93,178
Total current liabilities	9,236,195	9,274,043
Long-term debt	--	2,049,221
Commitments and contingencies		
Stockholders' equity:		
Preferred stock; $.001 par value; 5,000,000 authorized; no shares issued or outstanding	--	--
Common stock; $.001 par value; 30,000,000 shares authorized; 8,984,550 and 8,632,225 shares issues and outstanding at September 30, 1999 and December 31, 1998, respectively	37,131,042	35,009,368
Accumulated deficit	(25,078,428)	(27,514,682)
Total stockholders' equity	12,052,614	7,494,686
Total liabilities and stockholders' equity	$ 21,288,809	$ 18,817,950

See accompanying notes.

SONUS PHARMACEUTICALS, INC.
STATEMENTS OF OPERATIONS
(UNAUDITED)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	1999	1998	1999	1998
Revenues:				
Contract and licensing revenue	$ 10,000,000	$ 2,700,000	$ 12,050,000	$ 5,100,000
Operating expenses:				
Research and development	1,214,740	2,988,347	4,406,223	8,709,665
General and administrative	1,916,067	1,922,184	5,499,311	5,401,714
Total operating expenses	3,130,807	4,910,531	9,905,534	14,111,379
Operating income (loss)	6,869,193	(2,210,531)	2,144,466	(9,011,379)
Other income (expense):				
Interest income	63,471	231,118	355,662	776,706
Interest expense	(20,335)	(69,235)	(91,814)	(178,803)
Net income (loss)	$ 6,912,329	$ (2,048,648)	$ 2,408,314	$ (8,413,476)
Net income (loss) per share:				
Basic	$ 0.77	$ (0.24)	$ 0.27	$ (0.98)
Diluted	$ 0.76	$ (0.24)	$ 0.27	$ (0.98)
Shares used in computation of net income (loss) per share				
Basic	8,984,550	8,626,253	8,786,465	8,619,125
Diluted	9,089,663	8,626,253	8,932,683	8,619,125

See accompanying notes.

SONUS PHARMACEUTICALS, INC.
STATEMENTS OF CASH FLOWS
(UNAUDITED)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1999	1998
OPERATING ACTIVITIES:		
Net loss	$ 2,408,314	$ (8,413,476)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	508,613	627,959
Amortization of premium (discount) on marketable securities	(29,600)	(123)
Realized loss (gain) on marketable securities	5,139	(7,881)
Changes in operating assets and liabilities:		
Contract receivable	(5,000,000)	--
Other current assets	253,520	308,859
Accounts payable and accrued expenses	1,020,262	554,290
Accrued clinical trial expenses	(995,954)	(127,371)
Net cash used in operating activities	(1,829,706)	(7,057,743)
INVESTING ACTIVITIES:		
Purchases of equipment, furniture and leasehold improvements	(39,098)	(400,803)
Purchases of marketable securities	(15,350,254)	(23,419,722)
Proceeds from sale of marketable securities	12,613,763	17,772,969
Proceeds from maturities of marketable securities	7,049,147	13,292,590
Net cash provided by investing activities	4,273,558	7,245,034
FINANCING ACTIVITIES:		
Proceeds from bank line of credit	15,000,000	15,000,000
Repayment of bank line of credit	(15,000,000)	(15,000,000)
Increase in long-term debt	30,783	1,173,802
Repayment of capitalized lease obligations	(62,156)	(123,743)
Proceeds from issuance of common stock	41,668	134,824
Net cash provided by financing activities	10,295	1,184,883
Increase in cash and cash equivalents for the period	2,454,147	1,372,174
Cash and cash equivalents at beginning of period	5,203,925	5,253,227
Cash and cash equivalents at end of period	7,658,072	6,625,401
Marketable securities at end of period	7,490,663	13,690,045
Total cash, cash equivalents and marketable securities	$ 15,148,735	$ 20,315,446
Supplemental cash flow information:		
Conversion of long-term debt to equity	$ 2,080,005	$ --
Interest paid	$ 39,729	$ 50,584
Income taxes paid	$ --	$ 7,500

See accompanying notes.

SONUS PHARMACEUTICALS, INC.

NOTES TO FINANCIAL STATEMENTS
(UNAUDITED)

1. BASIS OF PRESENTATION

The unaudited financial statements of SONUS Pharmaceuticals, Inc. (the "Company") have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required to be presented for complete financial statements. The accompanying financial statements reflect all adjustments (consisting only of normal recurring items) which are, in the opinion of management, necessary for a fair presentation of the results for the interim periods presented.

The financial statements and related disclosures have been prepared with the assumption that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year. Accordingly, these financial statements should be read in conjunction with the audited financial statements and the related notes thereto included in the Form 10-K for the year ended December 31, 1998 and filed with the SEC on March 25, 1999.

2. LONG-TERM DEBT

Pursuant to the Company's collaborative agreement with Abbott Laboratories ("Abbott"), Abbott agreed to fund certain clinical trials of the Company during 1997 and 1998. Of the total clinical trial funding received from Abbott, 50% was to be paid back to Abbott within five years of the receipt of funds, plus accrued interest, in either cash or exchange for common stock of the Company at the then fair market value. In June 1999, the liability to Abbott of $2,080,005, representing 50% of clinical trial funding plus interest, was converted into 343,802 shares of common stock of the Company.

3. NYCOMED AGREEMENT

In the third quarter of 1999, the Company entered into a license agreement with Nycomed Imaging AS ("Nycomed") for the cross-license of certain proprietary ultrasound contrast agent technologies. Under the agreement, Nycomed has agreed to pay the Company a $10.0 million license fee, of which $5.0 million was received in September 1999 and the remaining $5.0 million was received in October 1999. In addition to the license fee, both companies have agreed to pay royalties to each other based on future sales of their respective ultrasound contrast agents. Under the terms of the agreement, the Company provides Nycomed with an exclusive license to the Company's ultrasound contrast patents except as related to perfluoropentane which is the gas used by the Company in its contrast products. Under the exclusive license to the patents, Nycomed also has the right to freely sublicense to other companies with a portion of any sublicense fees to be paid to the Company. In addition, the Company has a worldwide, non-exclusive license to certain of Nycomed's ultrasound contrast agent patents. The Company also has the right to sublicense these patents to its collaborative partners.

4. CONTINGENCIES

In May 1993, the Company entered into a manufacturing and supply agreement with Abbott. In the event that EchoGen(R) (perflenapent injectable emulsion) is approved by the U.S. Food and Drug Administration ("FDA"), the Company is obligated to purchase certain minimum quantities of materials from Abbott or make cash payments for the shortages from the predetermined purchase level over a five-year period.

In March 1998, the Company entered into a commercial supply agreement for certain medical grade raw materials for the Company's initial product in the U.S., EchoGen. In the event that EchoGen is approved by the FDA, the Company is obligated to purchase certain minimum quantities of the material over a five-year period.

The Company is also party to certain litigation related to its business. The Company notes that (i) litigation in general, and intellectual property and securities litigation in particular, can be expensive and disruptive to normal business operations, and (ii) the results of complex legal proceedings can be very difficult to predict with any certainty. There can be no assurance that these litigation proceedings will be resolved in the Company's favor. See "Part
II. Other Information; Item 1. Legal Proceedings."

5. SUBSEQUENT EVENT

In 1996, we entered into two agreements with Abbott for the marketing and selling of ultrasound contrast agents, including EchoGen, in: (1) the U.S. and;
(2) certain international territories including Europe, Latin America, Canada, Middle East, Africa and certain Asia/Pacific countries ("Abbott International Territories"). Subsequent to September 30, 1999, the Company and Abbott Laboratories International Division ("Abbott International") restructured their agreement related to the Abbott International Territories. The Company has commenced discussions with new potential marketing partners for the Abbott International Territories with the goal of having arrangements for certain countries in Europe in place by early 2000. Under the restructured agreement, Abbott International has returned all exclusive marketing rights to EchoGen to the Company. In addition, for the Abbott International Territories, the Company agreed to share with Abbott International, 21% of the Company's net profits from the sale of EchoGen and will also share 50% of any up-front license fees paid to the Company by new partners, of which 50% is credited against the share of net profits the Company will pay to Abbott International.

With the agreement Abbott International also retains a five-year option to elect to become a co-marketer of QW7437, the Company's second contrast agent under development. Abbott International has also agreed not to market or sell a competing ultrasound contrast product during the option period and thereafter, if it elects its option to co-market QW7437.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

In Management's Discussion and Analysis we explain the general financial condition and the results of operations for our Company, SONUS Pharmaceuticals, Inc., including:

o overview of our Company's business
o regulatory progress
o contractual agreements
o results of operations and why those results are different from the prior year period
o what capital resources our Company currently has and possible sources of additional funding for future capital requirements
o the market risk of our investment portfolio; and
o our progress related to the "Year 2000" issue

OVERVIEW

Our Company is engaged in the research, development and commercialization of ultrasound contrast agents and drug delivery systems based on our proprietary technology. Our products are being developed for use in the diagnosis and treatment of heart disease, cancer and other debilitating conditions. We have financed our research and development and clinical trials through payments received under contractual agreements, private equity and debt financings, and an initial public offering ("IPO") of common stock completed in October 1995. Clinical trials of our initial ultrasound contrast product under development, EchoGen(R) (perflenapent injectable emulsion), began in January 1994. In 1996, we filed a New Drug Application ("NDA") with U.S. Food and Drug Administration ("FDA") for EchoGen as well as a Marketing Authorization Application ("MAA") with the European Medicines Evaluation Agency ("EMEA").

REGULATORY PROGRESS

In April 1999, we received an "approvable letter" from the FDA for EchoGen. The FDA letter gave the conditions that must be satisfied before final approval. In September 1999, we filed a formal response to the conditions of the approvable letter. The FDA has notified us that it expects to complete its review on our response by March 2000. Although it is inappropriate for us to speculate on the outcome of the FDA review, we believe we have thoroughly addressed the conditions of the letter to achieve final approval. No assurance can be given that the FDA will review the response to the approvable letter in a timely manner or that the FDA will ultimately approve the NDA.

In March 1998, the EMEA's Committee for Proprietary Medicinal Products ("CPMP") issued a positive opinion on EchoGen for use as a transpulmonary echocardiographic contrast agent in patients with suspected or established cardiovascular disease who have had previous inconclusive non-contrast studies. In July 1998, the EMEA ratified the CPMP recommendation and granted a marketing authorization for EchoGen in the 15 countries of the European Union ("E.U."). We are seeking approval of variations to our marketing license to bring the manufacturing process and specifications for European product in line with the process and specifications submitted for approval with the FDA in the U.S. No assurance can be given that the variations to our marketing license will ultimately be approved.

CONTRACTUAL AGREEMENTS

In the third quarter of 1999, we entered into a license agreement with Nycomed Imaging AS ("Nycomed") for the cross-license of certain of our proprietary ultrasound contrast agent technologies. Under the agreement, Nycomed has agreed to pay us a $10.0 million license fee, of which $5.0 was received in September 1999 and the remaining $5.0 million was received in October 1999. In addition to

the license fee, both companies have agreed to pay royalties to each other based on future sales of our respective ultrasound contrast agents. Under the terms of the agreement, we provided Nycomed with an exclusive license to our ultrasound contrast patents except as related to perfluoropentane which is the gas we use in our contrast products. Under the exclusive license to the patents, Nycomed also has the right to freely sublicense to other companies with a portion of any sublicense fees to be paid to us. In addition, we have a worldwide, non-exclusive license to certain of Nycomed's ultrasound contrast agent patents. We also have the right to sublicense these patents to our collaborative partners.

In 1996, we entered into two agreements with Abbott Laboratories ("Abbott") for the marketing and selling of ultrasound contrast agents, including EchoGen, in: (1) the U.S. and; (2) certain international territories including Europe, Latin America, Canada, Middle East, Africa and certain Asia/Pacific countries ("Abbott International Territories"). Under these agreements, Abbott agreed to make certain payments to us, primarily conditioned upon the achievement of milestones, of which $37.7 million has been paid as of September 30, 1999. In addition, Abbott purchased in 1996, for $4.0 million, warrants to acquire 500,000 shares of our common stock. The warrants are exercisable over five years at $16.00 per share.

Subsequent to September 30, 1999, we and Abbott Laboratories International Division ("Abbott International") restructured our agreement related to the Abbott International Territories. We have commenced discussions with new potential marketing partners for the Abbott International Territories with the goal of having arrangements for certain countries in Europe in place by early 2000. Under the restructured agreement, Abbott International has returned all exclusive marketing rights to EchoGen to us. In addition, for the Abbott International Territories, we have agreed to share with Abbott International, 21% of our net profits from the sale of EchoGen and will also share 50% of any up-front license fees paid to us by new partners, of which 50% is credited against the share of net profits the we will pay to Abbott International. No assurance can be given that we will secure new marketing partners for the Abbott International Territories.

With the agreement Abbott International also retains a five-year option to elect to become a co-marketer of QW7437, our second contrast agent under development. Abbott International has also agreed not to market or sell a competing ultrasound contrast product during the option period and thereafter, if it elects its option to co-market QW7437.

RESULTS OF OPERATIONS

Our results of operations have varied and will continue to vary significantly from quarter to quarter and depend on, among other factors:

o timing of payments under contractual agreements
o timing of regulatory approvals
o entering into additional contractual agreements; and
o timing and costs of clinical trials

Abbott can terminate the U.S. agreement on short notice, and we cannot give assurance that we will receive any additional funding or milestone payments under the Abbott U.S. agreement.

To date, our reported revenues have been derived from payments received under contractual agreements with third parties. Revenue was $10.0 million for the third quarter of 1999 compared to $2.7 million in the prior year period. Revenue received in the third quarter of 1999 was derived from our agreement with Nycomed. Revenue received in the prior year period was derived from payments received under our agreements with Abbott. Revenue received for the nine months ended September 30, 1999 was $12.1 million compared to $5.1 million in the prior year period. Revenue for the nine months ended September 30, 1999 represents $10.0 million under our agreement with Nycomed and

$2.1 million under our agreements with Abbott. All revenue during the nine months ended September 30, 1998 represented payments under our agreements with Abbott.

Research and development expenses were $1.2 million for the third quarter of 1999 compared with $3.0 million for the same period of the prior year. Research and development expenses were $4.4 million for the nine months ended September 30, 1999 compared to $8.7 million in the prior year period. The decrease from the prior year periods was primarily due to a reduction in clinical trial activity on our products.

General and administrative expenses were $1.9 million for the third quarters of 1999 and 1998. General and administrative expenses were $5.5 million for the nine months ended September 30, 1999 compared to $5.4 million in the prior year period. The slight increase in the nine-month period was primarily due to an increase in intellectual property legal costs offset in part by decreases in marketing and medical education expenses.

We anticipate total operating expenses will increase in future quarters due to ongoing and planned clinical trials to study additional indications for EchoGen, future products and higher marketing and administrative expenses as we prepare for commercialization of EchoGen. We may also incur significant expenses relating to legal matters - see "Legal Proceedings."

Interest income, net of interest expense, was $43,000 for the third quarter of 1999 compared to $162,000 for the same period of the prior year and $264,000 and $598,000 for the nine months ended September 30, 1999 and 1998, respectively. The decrease in both periods was primarily due to the lower levels of invested cash.

LIQUIDITY AND CAPITAL RESOURCES

We have historically financed operations with payments from contractual agreements with third parties, proceeds from equity financings and our bank line of credit. At September 30, 1999, we had cash, cash equivalents and marketable securities of $15.1 million, compared to $17.0 million at December 31, 1998. The decrease was primarily due to cash used in operations during the nine-month period ended September 30, 1999.

We have a bank loan agreement which provides for a $5.0 million revolving line of credit facility and bears interest at the prime rate plus 1.0% per annum. At September 30, 1999 we had borrowings of $5.0 million outstanding under the line of credit. The line of credit expires August 30, 2000 and is secured by our tangible assets. In order to borrow under the line of credit, we are required to maintain certain minimum cash balances. We cannot give assurance that we will be able to maintain the minimum balances necessary to borrow under the line of credit.

We expect that our cash needs will increase significantly in future periods due to pending and planned clinical trials and higher administrative and marketing expenses as we prepare for commercialization of EchoGen, if and when approved for marketing. Based on our current operating plan, we estimate that existing cash and marketable securities will be sufficient to meet our cash requirements through the next 12 months. We may need to seek additional funding in 2000 through available means, which may include debt and/or equity financing or additional third party contractual agreements. We cannot give assurance that financing will be available on acceptable terms, if at all. Our future capital requirements depend on many factors including:

- the ability to obtain continued funding under existing contractual agreements
- the ability to attract and retain new partners
- the ability to maintain our bank line of credit
- the time and costs required to gain regulatory approvals
- the progress of our research and development programs and clinical trials

o the costs of filing, prosecuting and enforcing patents, patent applications, patent claims and trademarks
o the costs of marketing and distribution
o the status of competing products; and
o the market acceptance and third-party reimbursement of our products, if and when approved

We cannot give assurance that regulatory approvals will be achieved in the near-term or at all or that, in any event, additional financing will be available on acceptable terms, if at all. Any equity financing would likely result in substantial dilution to our existing stockholders. If we are unable to raise additional financing, we may be required to curtail or delay the development of our products and new product research and development, which could seriously harm our business.

YEAR 2000 COMPLIANCE

The "Year 2000" issue is the result of computer programs being unable to differentiate between the year 1900 and the year 2000 because computer code was written to recognize two digits rather than four digits to define the applicable year. This inability to recognize the correct century could result in system failures or miscalculation with respect to current software programs.

In response to the Year 2000 issue, we undertook a comprehensive review of our Company's business systems. We focused on the following four areas:

o software systems
o hardware systems
o facility systems
o significant third party vendors and business partners

Based on our review of these four areas, we believe that the Year 2000 issue does not pose significant operational problems. A majority of our software, computer and facilities equipment has been purchased within the last five years from third-party vendors who have already provided upgrades intended to bring their products into Year 2000 compliance. In addition, we surveyed significant vendors and business partners to determine any possible Year 2000 risks. The results of our survey determined that 93% of our vendors responded that they would be Year 2000 ready by December 31, 1999. For the 7% that failed to respond, we have developed contingency plans for their services. However, if unforeseen Year 2000 issues arise with these third parties, it could affect the ability of vendors to satisfy their obligations to us or for us to electronically communicate with such parties, which could have an adverse effect on our business, financial condition and results of operations.

We have established contingency plans to address "high-risk" processes and services that could affect day-to-day operations or delay our efforts to bring products to market if unforeseen Year 2000 issues arise. If needed, we are prepared and will have personnel on-site on January 1, 2000 to implement these contingency plans.

To date, based upon our review of the four areas noted above, we estimate that the full cost of correcting the Year 2000 issue will not exceed $100,000. While we believe we have brought our own systems into compliance and have been given assurance that critical third party relationships will be ready for the Year 2000, we cannot give assurance that we will not encounter unforeseen Year 2000 issues. If such issues are encountered, this could result in a material adverse effect on our business, financial condition and results of operations.

FORWARD-LOOKING STATEMENTS

This Report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and we intend that such forward-looking statements be subject to the safe harbors created thereby. Examples of these forward-looking statements include, but are not limited to:

o the submission of applications for and the timing or likelihood of marketing approvals for one or more indications
o market acceptance of our products
o our anticipated future capital requirements and the terms of any capital financing
o the progress and results of clinical trials
o the timing and amount of future payments under contractual agreements; and
o the anticipated outcome or financial impact of legal matters

While these statements made by us are based on our current beliefs and judgement, they are subject to risks and uncertainties that could cause actual results to vary.

In evaluating such statements, stockholders and investors should specifically consider a number of factors and assumptions, including those discussed in the text and the financial statements and their accompanying footnotes in this Report and the risk factors detailed from time to time in our filings with the Securities and Exchange Commission. As discussed in our Annual Report on Form 10-K for the year ended December 31, 1998, actual results could differ materially from those projected in the forward-looking statements as a result of the following factors, among others:

o uncertainty of governmental regulatory requirements and lengthy approval process
o unproven safety and efficacy of products and uncertainty of clinical trials
o history of operating losses and uncertainty of future financial results
o future capital requirements and uncertainty of additional funding
o dependence on third parties for funding, clinical development and distribution
o dependence on patents and proprietary rights
o competition and risk of technological obsolescence
o limited manufacturing experience and dependence on limited contract manufacturers and suppliers
o lack of marketing and sales experience
o limitations on third-party reimbursement
o uncertainty of market acceptance
o continued listing on the Nasdaq National Market
o uncertainty of legal matters
o dependence on key employees; and
o shares eligible for future sale

There can be no assurance that we can meet the conditions set forth by the FDA in its "approvable letter" or any subsequent conditions in a timely manner, if at all, or that EchoGen will ultimately receive FDA approval.

ITEM 3. MARKET RISK

There has been no material change during the quarter ended September 30, 1999, from the disclosures about market risk provided in our Annual Report on Form 10-K for the year ended December 31, 1998.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In January 1998, we announced that we had filed a patent infringement action in the U.S. District Court in Seattle, Washington, against Molecular Biosystems Inc. ("MBI") and Mallinckrodt Medical. The suit alleges that one of MBI's ultrasound contrast agents infringes one or more of our patents. MBI has filed counterclaims alleging that the patents asserted by us are invalid and not infringed, and that we have made false public statements and engaged in other actions intended to damage MBI and one of its ultrasound contrast agents. We do not believe there is any merit to these counterclaims and intend to defend our position vigorously. In October 1998, the court granted our motion to stay the litigation until the U.S. Patent and Trademark Office ("PTO") had completed its re-examination of the patents in this lawsuit (see below). The stay was lifted in January 1999. A trial date has been set for this lawsuit in April 2000.

Under the agreement between Nycomed Imaging AS ("Nycomed") and SONUS, Nycomed is an exclusive licensee of our patents in a field of use including non-perfluoropentane ultrasound contrast agents. Nycomed has the right to control the patent infringement portion of our lawsuit against MBI and Mallinckrodt Medical. The court has authorized Nycomed to be joined as a party in this lawsuit.

Four separate re-examination proceedings directed to the two SONUS patents at issue in the patent infringement lawsuit, U.S. 5,558,094 (`094) and U.S. 5,573,751 (`751) were initiated by the PTO beginning in July 1997 at the request of MBI. In December 1998, we announced that we received decisions from the PTO indicating the patentability of claims in all four re-examination proceedings. The PTO confirmed the patentability of a number of the claims included in the original `094 and `751 patents as well as some claims that were amended during re-examination, and has issued re-examination certificates for each patent. Certain claims, which included reference to fluorinated chemicals other than perfluoropropane, perfluorobutane and perfluoropentane, were cancelled during the re-examination process.

In August and September 1998, various class action complaints were filed in the Superior Court of Washington (the "State Action") and in the U.S. District Court for the Western District of Washington (the "Federal Action") against SONUS and certain of our officers and directors, alleging violations of Washington State and U.S. securities laws. In October 1998, we, and the individual defendants, moved to dismiss and stay the State Action. In the State Action state law claims were later brought in the Federal Action and the State Action was dismissed. In February 1999, plaintiffs filed a consolidated and amended complaint in the Federal Action, alleging violations of Washington State and U.S. securities laws. In March 1999, we, and the individual defendants, filed a motion to dismiss the consolidated amended complaint in the Federal Action. In July 1999, the Court entered an order denying in part and granting in part the motion to dismiss the complaint in the Federal Action. In November 1999, we filed motions for summary judgement and to stay discovery. These motions are currently scheduled for hearing in December 1999. We do not believe there is any merit to the claims in these actions and we intend to defend our position vigorously. Although we do not believe that we or any of our current or former officers or directors have engaged in any wrongdoing, there can be no assurance that this stockholder litigation will be resolved in our favor.

ITEM 5. OTHER EVENTS

In August 1999, the Company entered into an Agreement for Part-Time Employment and Mutual Release with the Company's founder and former Chief Executive Officer, Steven C. Quay, M.D., Ph.D. Under the agreement, Dr. Quay will provide services to the Company as a part-time employee for a period of three years from the date of the agreement. In September 1999, Dr. Quay resigned as a member of the Company's Board of Directors.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) EXHIBITS

Number	Description
10.21C	Loan Modification Agreement dated August 30, 1999 to Loan and Security Agreement by and between the Company and Silicon Valley Bank
10.37	Agreement for Part-time Employment and Mutual Release, effective August 25, 1999 by and between the Company and Steven C. Quay, M.D., Ph.D.
10.38	Mutual Rescission Agreement dated October 11, 1999 by and between the Company and Abbott International, Ltd.
27.1	Financial Data Schedule

(b) REPORTS ON FORM 8-K

We filed a report on Form 8-K on October 14, 1999 in connection with the closing on September 28, 1998 of our License Agreement with Nycomed Imaging AS.

ITEMS 2, 3 AND 4 ARE NOT APPLICABLE AND HAVE BEEN OMITTED.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SONUS PHARMACEUTICALS, INC.

Date: February 29, 2000	*By: /s/ Gregory Sessler* *---* *Gregory Sessler* *Senior Vice President - Strategic Business Development and Chief Financial Officer* *(Principal Financial Officer)*

Exhibit 10.21C
LOAN MODIFICATION AGREEMENT

This Loan Modification Agreement is entered into as of August 30, 1999, by and between Sonus Pharmaceuticals, Inc. ("Borrower") and Silicon Valley Bank ("Silicon").

1. DESCRIPTION OF EXISTING INDEBTEDNESS: Among other indebtedness which may be owing by Borrower to Silicon, Borrower is indebted to Silicon pursuant to, among other documents, a Loan and Security Agreement, dated August 11, 1995, together with all Schedules attached thereto, as such agreement may be amended from time to time (the "Loan Agreement"). The Loan Agreement provided for, among other things, a Secured Line of Credit in the original principal amount of Five Million and 00/100 Dollars ($5,000,000.00). Capitalized terms used but otherwise defined herein shall have the same meaning as in the Loan Agreement.

Hereinafter, all indebtedness owing by Borrower to Silicon shall be referred to as the "Indebtedness".

2. DESCRIPTION OF COLLATERAL AND GUARANTIES. Repayment of the Indebtedness is secured by the Collateral as defined in the Loan Agreement.

Hereinafter, the above-described security documents and guaranties, together with all other documents securing repayment of the Indebtedness shall be referred to as the "Security Documents". Hereinafter, the Security Documents, together with all other documents evidencing or securing the Indebtedness shall be referred to as the "Existing Loan Documents".

3. DESCRIPTION OF CHANGE IN TERMS.

A. Modification(s) to Loan Agreement.

1. The defined term "Maturity Date" shall mean August 30, 2000, at which time all unpaid principal and accrued but unpaid interest shall be due and payable.

2. Beginning with the month ending September 30, 1999, the paragraph entitled "Minimum Cash Balance" under paragraph entitled "Other Covenants" shall be amended to read as follows:

Borrower shall maintain at all times cash and cash equivalents of not less than $10,000,000 net of outstanding advances under the Credit Limit. However, if Borrower has less than $10,000,000 but more than $4,000,000, any advance of the funds under Credit Limit shall be subject to the following conditions:

(i) any advance of funds under the Credit Limit shall be deposited directly into Borrower's account with Silicon. Such account will only be allowed access to use for paying down the amounts outstanding under the Credit Limit; and

(ii) Borrower shall pay Silicon an additional fee in the amount of Two Thousand Five Hundred and 00/100 Dollars ($2,500.00).

4. CONSISTENT CHANGES. The Existing Loan Documents are hereby amended wherever necessary to reflect the changes described above.

5. PAYMENT OF LOAN FEE. Borrower shall pay to Silicon a fee in the amount of Fifteen Thousand and 00/100 Dollars ($15,000.00) (the "Loan Fee") plus all out-of-pocket expenses.

6. NO DEFENSES OF BORROWER. Borrower (and each guarantor and pledgor signing below) agrees that it has no defenses against the obligations to pay any amounts under the Indebtedness.

7. CONTINUING VALIDITY. Borrower (and each guarantor and pledgor signing below) understands and agrees that in modifying the existing Indebtedness, Silicon is relying upon Borrower's representations, warranties, and agreements, as set forth in the Existing Loan Documents. Except as expressly modified pursuant to this Loan Modification Agreement, the terms of the Existing Loan Documents remain unchanged and in full force and effect. Silicon's agreement to modifications to the existing Indebtedness pursuant to this Loan Modification Agreement in no way shall obligate Silicon to make any future modifications to the Indebtedness. Nothing in this Loan Modification Agreement shall constitute a satisfaction of the Indebtedness. It is the intention of Silicon and Borrower to retain as liable parties all makers and endorsers of Existing Loan Documents, unless the party is expressly released by Silicon in writing. Except as otherwise expressly provided herein, no maker, endorser, or guarantor will be released by virtue of this Loan Modification Agreement. The terms of this paragraph apply not only to this Loan Modification Agreement, but also to all subsequent loan modification agreements.

8. CONDITIONS. The effectiveness of this Loan Modification Agreement is conditioned upon Borrower's payment of the Loan Fee.

This Loan Modification Agreement is executed as of the date first written above.

BORROWER: SILICON:

SONUS PHARMACEUTICALS SILICON VALLEY BANK

By: /s/ Gregory Sessler	*By: /s/Peter Palsson*
---	*---*
Name: Gregory Sessler	*Name: Peter Palsson*
Title: Chief Financial Officer	*Title: Vice-President*

EXHIBIT 10.37

AGREEMENT FOR PART-TIME EMPLOYMENT AND MUTUAL RELEASE

This Agreement for Part-Time Employment and Mutual Release is made and entered into by and between Sonus Pharmaceuticals, Inc., a Delaware corporation (the "Company"), and Steven C. Quay, M.D., Ph.D., an individual ("Dr. Quay"), as of this 25th day of August, 1999.

RECITALS

WHEREAS, Dr. Quay was the founder of the Company and served as its Chief Executive Officer since its inception in 1991; and

WHEREAS, Dr. Quay is the inventor of certain inventions within the Company's intellectual property estate; and

WHEREAS, Dr. Quay is holder of a substantial amount of the Company's common stock; and

WHEREAS, Dr. Quay and the Company were party to an Employment Agreement dated February 11, 1999 (the Employment Agreement"), which, except as relates to its paragraphs 6, 7 and 9 as provided herein, has been terminated and is no longer in force and effect; and

WHEREAS, Dr. Quay and the Company desire to resolve amicably all disputes and controversies between them and enter a Mutual Release; and

WHEREAS, the Company desires Dr. Quay to provide services for it as a part-time employee; and

WHEREAS, Dr. Quay desires to provide services to the Company as a part-time employee;

NOW, THEREFORE, in consideration of the premises and the mutual covenants and agreements set forth herein, Dr. Quay and the Company, intending to be legally bound, hereby agree as follows:

1. Part-Time Employment. Dr. Quay will, as a part-time employee, provide services to the Company or to others such as Nycomed Imaging A/S as reasonably directed by the Company consistent with the terms of this Agreement, for a period of thirty-six (36) months on such projects which are consistent with Dr. Quay's expertise and which are reasonably requested by the Company from time to time, pertaining to the following: (A) obtaining issuance of suitable patents on its currently pending patent applications, as well as subsequent continuation or continuation-in-part applications of the Company, and any applications that may be filed by or for the Company on recent discoveries relating to * (herein, collectively, the "Sonus Patents"), including providing assistance in connection with proceedings in the U.S. Patent and Trademark Office, (B) asserting rights

* Confidential portions omitted and filed separately with the Commission.

against potential infringers of the Sonus Patents, including providing cooperation and assistance in proceedings and litigation relating thereto, (C) participating and providing assistance in the design and development of research projects and associated intellectual property strategies relating to the Sonus Patents, and (D) participating and providing assistance in strategies relating to licensing and maximizing the economic value of the Company's intellectual property estate as it currently exists. Dr. Quay's activities may address other matters as the parties may mutually agree.

(A) Through December 31, 1999, Dr. Quay will be available to provide these services for up to 144 hours per calendar quarter (or a pro rata amount for any partial calendar quarter) as requested by the Company consistent with "C" below. During the remainder of the part-time employment, Dr. Quay will be available for up to 80 hours per calendar quarter (or a pro rata amount for any partial calendar quarter) as requested by the Company consistent with "C" below.

(B) In consideration for providing these services, Dr. Quay will receive salary/wages as follows:

(i) Through December 31, 1999, Dr. Quay will receive his salary in effect under the Employment Agreement on and prior to July 7, 1999, payable on the normal Company pay days (and the Company shall pay Dr. Quay on the first pay day after execution of this Agreement an amount equal to any unpaid salary for any portion of 1999 to the date of this Agreement) so that, by the end of 1999, or by the first regular Company pay day thereafter, Dr. Quay shall have received an amount of salary paid heretofore to him in the first portion of 1999 and to be paid to him hereunder for the second portion of 1999 equal to what his salary would have been for all of 1999 under the Employment Agreement.

(ii) For the remainder of the part-time employment, Dr. Quay shall receive wages in the amount of $250 per hour for services requested by the Company, with a minimum service period of one hour per inquiry (i.e. for each request by the Company and each additional inquiry by the Company requiring separate devotion of time by Dr. Quay).

(C) The Company and Dr. Quay shall work together in scheduling his services as a part-time employee at times mutually convenient to Dr. Quay and the Company and which will accommodate Dr. Quay's other commitments and activities. Dr. Quay will generally provide these services from his home or other location of his choice during regular business hours. Subject to such accommodation, the Company may request, from time to time, that Dr. Quay provide the services at other locations or travel to other locations; for example, in connection with negotiations or proceedings with third parties. In connection with the rendering of any services as a part-time employee, travel time shall be considered employment time and Dr. Quay will be reimbursed for all of his reasonable travel, lodging, meals and other expenses

upon submission of reasonable documentation thereof and subject to such reasonable limitations on first class travel or accommodations as the Company may impose on all of its executive officers and directors and communicate in writing to Dr. Quay.

2. Stock Options. The Company confirms that during Dr. Quay's part-time employment hereunder those options under Dr. Quay's existing stock option agreements (which shall remain in full force and effect) will continue to vest and will remain exercisable for the period of such part time employment and for the period thereafter provided in such option agreements. Dr. Quay shall not be deemed a full-time employee under the Change in Control Agreement dated February 11, 1999 and, accordingly, that agreement shall be deemed to have terminated as of July 7, 1999.

3. Benefits. Dr. Quay will retain the employee welfare benefits under the Company's health, dental or other welfare benefit plans (or the equivalent thereof), through December 31, 1999. Dr. Quay will be deemed to satisfy a 24 hour or more per week requirement under such plans. After December 31, 1999, Dr. Quay and his family may continue such coverage at his/their own expense if and for as long as such coverage may be permitted under COBRA.

4. Dr. Quay's Shares of Common Stock of Sonus.

(A) Dr. Quay confirms that for so long as he remains a Director of the Company, he shall be subject to the Company's uniform blackout policies regarding sales of shares by insiders to the extent they are applicable to all Directors. The Company represents: (i) that those policies, as currently in effect and applicable to all directors, are set forth in Exhibit A hereto; (ii) that the Company will provide Dr. Quay promptly after the date hereof with revised versions of Exhibit A which shall set forth such policies applicable to all Directors with any changes and amendments as may be made from time to time and any exceptions as may be made for any other Directors; (iii) that such policies shall be enforced uniformly as to all Directors. In addition, to the extent that Dr. Quay is aware of or possesses material inside information as a result of his directorship or part-time employment with the Company, he shall comply with all applicable securities laws.

(B) In the event Dr. Quay desires to sell any of his shares of common stock of the Company, including without limitation, shares of common stock issuable upon exercise of options, the Company and Dr. Quay agree to mutually consult and cooperate in effecting any such resales of shares by Dr. Quay with a view to minimizing any material adverse impact on the market for the shares to the extent practicable, provided that the Company shall not be entitled to block or prevent sales Dr. Quay intends to make consistent with paragraph (A) above. In this regard, the Company agrees to use its reasonable efforts to assist Dr. Quay in any such sales, including without limitation, facilitating off-market block trades with the assistance of the Company's market makers. In addition, the parties agree to mutually consult on a

continual basis as to means and methods by which sales of shares of common stock may be most readily made consistent with obtaining the best price and not materially adversely impacting the market price and otherwise render reasonable assistance to Dr. Quay in connection therewith.

(C) The Company confirms the existing Fourth Amended and Restated Registration Rights Agreement dated 1999 ("Registration Rights Agreement") as it applies to shares of common stock held by Dr. Quay. In addition, the Company confirms the effectiveness of one or more S-8 registration statements relating to the shares of common stock subject to options held by Dr. Quay; it being understood, however, that such S-8 registration statements may not be available for resale of shares by "affiliates" as provided under the Securities Act of 1933, as amended, and regulations thereunder (collectively, the "Act"). The Company agrees to use its commercially reasonable best efforts to maintain the effectiveness of such registration statements. In the event that Dr. Quay wishes to sell shares of the Company in a manner not available to an "Affiliate" as defined under the Act, he will so inform the Company. In such event, if the Company, after consultation with counsel, advises Dr. Quay in writing that it believes in good faith that "Affiliate" status under the Act quite possibly continues to exist as to Dr. Quay, Dr. Quay may provide to the Company an opinion of counsel (which may be from Blanc Williams Johnston & Kronstadt, LLP, or other counsel reasonably acceptable to the Company), stating that Dr. Quay is not, at that time, an "Affiliate" under the Act, and the Company will act accordingly. The Company shall pay fifty percent (50%) of the reasonable costs actually incurred in obtaining such legal opinion. The Company agrees not to assert that Dr. Quay is an "Affiliate" of the Company under the Act solely because of his part-time employment with the Company.

(D) In the event that the Company proposes to effect any private placement of shares in a capital raising transaction, during the term of this Agreement for Part-Time Employment, the Company shall use its reasonable efforts to include a portion of the shares of common stock held by Dr. Quay to the extent practical; provided, however, that the Company shall have no obligation to include such shares held by Dr. Quay to the extent (i) the Company certifies in writing to Dr. Quay that such inclusion would have a materially adverse impact on the Company's working capital requirements or jeopardize the Company's satisfaction of listing requirements under the Nasdaq National Market System or (ii) the placement agent retained by the Company in connection with the private placement certifies in writing to Dr. Quay that such inclusion would otherwise jeopardize the completion of the private placement.

5. Publicity. The parties hereby agree not to disparage each other. In addition, neither party shall make any public announcement relating to the transactions provided for herein or the change of Dr. Quay's relationship with the Company from full-time to part-time employment without the prior written consent of the other party, which shall not be unreasonably withheld; provided, however, that the Company may, after affording Dr. Quay 48 hours after his receipt thereof to review and comment, make such public disclosures concerning these matters as may be required under the applicable securities laws, including without limitation, the filing of this Agreement as an exhibit to the Company's filings under the Act if it first provides Dr. Quay with written advice from its securities counsel that such counsel, after review, believes such

filing is required.

6. Covenants Against Actions Damaging the Company; Noncompetition. Dr. Quay hereby confirms that the covenants set forth in paragraphs 6, 7 and 9 of the Employment Agreement remain in full force and effect during the 36 month term of part-time employment and for the periods thereafter as specifically provided in such sections, except that Dr. Quay shall not be required to disclose to the Company any inventions which he develops or discovers during the term of this Agreement for Part-Time Employment or thereafter. In addition, for the purposes of paragraph 9, the business of the Company shall mean ultrasound contrast agents and Vitamin E emulsion technology for drug delivery (hereinafter referred to as the "Business"); and Dr. Quay shall not be deemed to be in violation of the paragraph 9 non-compete merely because of entering into a business arrangement, including a licensing, partnership, employment, consulting, agency or similar arrangement, with an established entity whose business does not primarily consist of but includes activities competitive with the Business, provided that Dr. Quay's activities with respect to such entity do not directly or indirectly relate to the Business. Dr. Quay confirms that the provisions of paragraph 9 of the Employment Agreement shall preclude any activities by Dr. Quay that may assist any third party in challenging the patents or intellectual property estate of the Company, provided however, that truthful testimony given by Dr. Quay pursuant to subpoena, court order or other compulsory legal process shall not violate the provisions of paragraph 9 of the Employment Agreement and, provided further, that nothing herein is intended to prevent Dr. Quay from providing truthful testimony pursuant to such process. Dr. Quay further specifically agrees not to assist or otherwise take any actions on behalf of any third party that are adverse to the Company with respect to the Sonus Patents or that are adverse, with respect to the Sonus Patents, to the Company's current or future licensees and/or licensors, in any litigation or administrative proceeding relating to those Patents. The Company acknowledges that it has been provided with a copy of U.S. Patent No. 5,798,266, entitled, "Methods and Kits for Obtaining and Assaying Mammary Fluid Samples from Breast Diseases, Including Cancer," Inventors: Quay, SC, Quay DL; issued August 25, 1998 (assigned to K-QUAY Enterprises, LLC, a Delaware LLC formed by Dr. Quay) and has asserted no interest therein.

7. Mutual Releases. Except for the obligations arising under this Agreement (including the provisions of paragraphs 6, 7 (as amended above) and 9 (as amended above) of the Employment Agreement and the Registration Rights Agreement and the stock option agreements described in Section 2 above) and the indemnity agreement between Dr. Quay and the Company, (and any indemnity provisions in the Company's charter documents) Dr. Quay, for himself and for his heirs, executors, legal successors and assigns, hereby releases and absolutely and forever discharges the Company and its affiliates, and each of their respective past and present officers, directors, shareholders, employees, insurers, attorneys and agents, and each of them, and each of their respective legal predecessors, successors and assigns ("Sonus Releasees") of and from any and all claims, demands, promises, contracts, damages, debts, liabilities, accounts, costs, actions and causes of action of every kind and nature, whether now known or unknown, accrued or unaccrued, suspected or unsuspected, matured or unmatured, liquidated or unliquidated, contingent or noncontingent, which he may now have, has had, or may hereafter have against Sonus Releasees arising out of any matter or event occurring prior to the date of this Agreement,

including but not limited to, claims arising out of or with respect to the Employment Agreement, his employment by the Company and/or other Sonus Releasees, and any purported termination of such employment thereafter, including (a) any discrimination claim, or (b) any claim, known or unknown, for wrongful termination, or (c) any other claim, whether in tort, contract or otherwise; and the Company and its affiliates, for themselves and their respective legal predecessors, successors and assigns, hereby release and absolutely and forever discharge Dr. Quay and his heirs, legal successors, assigns, of and from any and all claims, demands, damages, promises, contracts, debts, liabilities, accounts, costs, actions and causes of action of every kind and nature, whether now known or unknown, accrued or unaccrued, suspected or unsuspected, matured or unmatured, liquidated or unliquidated, contingent or noncontingent, which they may now have, have had, or may hereafter have against Dr. Quay and his heirs, legal successors, assigns, insurers, attorneys, and/or agents, and each of them and each of their respective legal predecessors, successors and assigns arising out of any matter or event occurring prior to the date of this Agreement including but not limited to, all claims whether in tort, contract or otherwise. The Company represents that as of the date hereof, it does not have knowledge of any claim or facts giving rise thereto, against Dr. Quay under the Sections 6, 7 or 9 of the Employment Agreement.

Dr. Quay and the Company hereby agree that they will not make, assert or maintain against any entity or person that has been released in this Agreement, any claim, demand, action, suit or proceeding thereof, arising out of or in connection with the matters herein so released. Furthermore, Dr. Quay and the Company hereby represent and warrant that they have not heretofore assigned or transferred or purported to assign or transfer to any person, firm, or other entity, any claim, demand, debt, liability, account, cost, action or cause of action hereinabove released.

The parties hereto acknowledge that statutory and/or case law in some states limits the effectiveness of releases of unknown claims. Nevertheless, they have bargained for such a broad and effective release and hereby waive the benefits of such statutory and/or case law, intending that the above releases have broad effect consistent with their wording.

8. Miscellaneous Provisions.

(A) Notices. Any notice given hereunder to the Company or to Dr. Quay shall be deemed sufficiently given if mailed by registered or certified mail, return receipt requested, postage prepaid, or sent by overnight delivery service, or by facsimile (with machine confirmation and hard copy following by mail) as follows:

If to the Company:

Sonus Pharmaceuticals, Inc.
22026 Twentieth Avenue, S.E.
Bothell, WA 98021
Attention: President and Chief Executive Officer

Facsimile number: 425 489-3936

If to Steven C. Quay, M.D., Ph.D.:

23632 Highway 99, Suite F-454
Edmonds, WA 98026

Facsimile number: [603] 816-9696

or to such other address or fax number as shall have been provided by the party to whom such notice is directed by notice to the other party hereto in accordance with this section. Except as otherwise provided herein, such notice shall be deemed effective when delivered in person (including by express courier), when sent by facsimile (with machine confirmation and with hard copy following by mail) or three days after being mailed.

(B) Governing Law. This Agreement is made under and shall be governed by and construed in accordance with the laws of the State of Washington, applicable to agreements made between residents of that state and providing for performance there.

(C) Assignment. Neither this Agreement nor any duties or obligations under this Agreement may be assigned to by either party without the prior written consent of the other party, provided however, the Company may assign this Agreement in connection with any sale or transfer of the business to which it relates, whether by merger, sale of assets, sale of stock or otherwise.

(D) Attorneys' Fees. If any action is brought to enforce or interpret the provisions of this Agreement, the prevailing party in such action will be entitled to its reasonable attorneys' fees and costs incurred, in addition to any other relief to which such party may be entitled.

(E) Waiver of Breach. The waiver of either party of a breach of any provision of this Agreement shall not operate or be construed as a waiver of any subsequent breach of this Agreement.

(F) Severability. To the extent any provision of this Agreement shall be invalid or unenforceable, it shall be considered deleted herefrom and the remainder of such provision and of this Agreement shall be unaffected and shall continue in full force and effect. In furtherance and not in limitation of the foregoing, should the duration or the geographical extent of or business activities covered by any provision of this Agreement be in excess of that which is valid and enforceable under applicable law, then such provision shall be construed to cover only the maximum duration, extent or activities which may validly and enforceably be covered under applicable law. Dr. Quay acknowledges the uncertainty of the law in this respect and expressly stipulates that this Agreement shall be given the construction which renders its provisions valid and enforceable

to the maximum extent (not exceeding its express terms) possible under applicable law.

(G) Authority. Each individual signing for each of the parties herein warrants and represents that he is an authorized agent of such party, for whose benefit he is executing this Agreement, and is authorized to execute the same.

(H) Further Assurances. Each party agrees to execute such other and further instruments and documents as may be necessary or proper in order to complete the transactions contemplated by this Agreement.

(I) Amendments. No amendment or modification of this Agreement shall be deemed effective unless made in writing signed by the parties hereto.

(J) Counterparts. This Agreement may be executed and delivered by facsimile, in which case it shall be effective when so executed and delivered, and the parties agree to exchange hard copy signature pages as soon thereafter as feasible. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one in the same instrument.

(K) Integration. Dr. Quay and the Company agree that this Agreement for Part-Time Employment and Mutual Release is the sole agreement between them regarding the subject matter herein and embodies all terms, promises, representations, and understanding regarding the subject matter herein, and that no representations, inducements, or promises have been made except as expressly stated herein.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date and year set forth above.

SONUS PHARMACEUTICALS, INC., a Delaware
corporation

By: /s/ Michael A. Martino

Michael A. Martino, President and
Chief Executive Officer

STEVEN C. QUAY, M.D., Ph.D.

/s/ Steven C. Quay

EXHIBIT 10.38

October 11, 1999

Michael A. Martino
President and Chief Operating Officer
SONUS Pharmaceuticals, Inc.
22026 20th Avenue, S.E.
Bothell, WA 98021

RE: International License Agreement dated October 1, 1996

Dear Mr. Martino:

This letter is to confirm our mutual decision to rescind the International License Agreement dated October 1, 1996 between Abbott International, Ltd., a Delaware corporation with principal offices at 100 Abbott Park Rd., Abbott Park, IL 60064-3500 ("Abbott") and SONUS Pharmaceuticals, Inc., a Delaware corporation with principal offices at 22026 20th Avenue, S.E., Suite 102, Bothell, WA 98021 ("Sonus"), as amended by the First Amendment dated January 31, 1999, as well as the Trademark License Agreement between Sonus and Abbott referenced therein (collectively referred to herein as "the International Agreement"), in consideration of the premises and the mutual promises and covenants set forth in this letter. The consideration for our mutual decision to rescind includes, but is not limited to, the relinquishment of disputed claims and the resolution of outstanding issues between the parties arising from the International Agreement. Unless otherwise defined herein, all capitalized terms shall have the meanings ascribed to such terms under the International Agreement. This rescission is effective as of the date of this letter and as of such date, Sonus and Abbott shall not have any further liability or obligation to each other, financial or otherwise, except as expressly set forth in this letter.

1. For a period of ten (10) years from the date of this letter, Sonus and Abbott shall indemnify, defend and hold harmless each other from and against all claims, causes of action, settlement costs (including reasonable attorney's fees and expenses), losses or liabilities of any kind which (a) are asserted by a third party, (b) arise from or are attributable to any negligent act or omission or willful misconduct on the part of Sonus or Abbott (as the case may be) or their respective directors, employees, agents or representatives, and (c) which relate to (i) the obligations, representations and warranties of Sonus or Abbott
(as the case may be) under the International Agreement or this letter, or (ii) the mutual decision of Sonus and Abbott to rescind the International Agreement, or (iii) any public statement or disclosure relating to the International Agreement or the subject matter thereof or this letter of the subject matter hereof. Any party seeking indemnification ("the indemnified party") under this paragraph shall promptly notify the other party ("the indemnifying party") in writing and

shall fully cooperate with the indemnifying party in the defense of such claim. If the indemnifying party wishes to enter into any settlement, consent to any judgment, or otherwise resolve such claim in any manner which includes any obligation, loss, or cost to the indemnified party, the indemnifying party must first obtain the written consent of the indemnified party before finalizing such settlement, judgment or resolution.

2. Except for third party liability arising under section 1 above, in no event shall Sonus or Abbott be liable for loss of profits or other economic loss, or for indirect or incidental penalties or consequential damages, or other similar damages arising out of anything relating to the International Agreement or the subject matter thereof, or to this letter or the subject matter hereof.

3. Within thirty (30) days of the date of this letter, Sonus and Abbott shall return or destroy all Confidential Information provided to each other under the International Agreement or the Confidential Disclosure Agreement between the parties dated August 6, 1996 ("CDA"), and for a period of five (5) years from the date of this letter, neither party shall use or disclose the other party's Confidential Information, except that: (a) each party may retain one archival copy of such Confidential Information; and (b) any Confidential Information which was also provided under any other agreement presently in effect between Sonus and Abbott Laboratories may be retained and used by Sonus and Abbott Laboratories under the terms and conditions of such agreement(s).

4. For a period of ten (10) years from the date of this letter, neither Sonus nor Abbott shall (a) originate any publicity, news release or other public announcement or make any public statement or response to questions, written or otherwise, whether to the public press, stockholders, investment analysts or otherwise, relating to the Confidential Information, to the International Agreement or the subject matter thereof or to this letter or the subject matter hereof, or (b) use the name of the other party in any publicity, news release, public statement or response or other announcement, except (i) with the prior written consent of the other party after affording such other party no less than three (3) business days to review such proposed disclosure, or (ii) as required by law, regulation or court order, in which case the originating party shall give the other party no less than three (3) business days notice of such proposed disclosure and the reason(s) requiring it so that the other party may review the proposed disclosure and determine its response to such proposed disclosure, provided that, if the operation of law, regulation or court order requiring such disclosure does not allow the disclosing party itself three (3) business days notice, the disclosing party shall give the other party as much prior written notice as is practicable. The disclosing party shall, if requested by the other party in the event of a proposed disclosure under subparagraph
(4)(ii) above, fully cooperate with the other party in taking or in assisting the other party to take any actions, consistent with applicable law, which the other party deems necessary or desirable to prevent, protect or modify the disclosure. Consent by either party to a specific public disclosure shall also be deemed to be consent to future disclosures of the same facts.

5. Promptly following the date of this letter, Abbott shall cooperate in good faith with Sonus to transition the duties and responsibilities of Abbott under the International Agreement to Sonus as described in this Section 5. Within ninety (90) days of the date of this letter, Abbott shall deliver to Sonus the following:

* Confidential portions omitted and filed separately with the Commission.

(i) all clinical trial data, reports and protocols prepared by or on behalf of Abbott in connection with the International Agreement; and

(ii) all filings, written information and materials relating to the approval for price and reimbursement of the Product with all regulatory agencies located in the Territory.

6. Subject to the provisions of sections 7 and 8 below, for a period of three (3) years from the date of this letter, Sonus may request that Abbott provide to Sonus, for the benefit of Sonus and/ or Sonus's designated third-party partners or distributors for the Product ("Sonus Partners"), certain services in connection with the Product, as set forth in the following subsections. For the purposes of this letter, "Product" means a colloidal dispersion ultrasound agent for intravenous injection containing the active ingredient dodecafluoropentane, constituted as the product Echogen(R) in the form for which Sonus has received marketing authorization in the European Union (the "EU"). If Sonus so requests, then within the same three (3) year period, Abbott shall provide such services (or similar lesser services as the parties may agree, always provided that Abbott shall not be required to provide greater or additional services beyond those set forth in the subsections below).

(a) Upon the request of Sonus, Abbott shall transport the Product intended for sale in the EU, from Abbott Laboratories's manufacturing *. The Product shall then be held at such distribution center to be ready for pickup by or further transport arranged by, and at the cost of, Sonus and/or Sonus Partners, provided that Abbott shall not be required to release any such Product to Sonus or any third party unless and until Abbott has (i) determined in its reasonable discretion that such Product is acceptable for release under applicable regulatory provisions and under the test results resulting from the testing performed under Paragraph 6(b) below, and (ii) received written instructions from Sonus which are sufficient to enable Abbott properly to identify the Sonus Partner(s) to whom Abbott is to release the Product and the amount of Product to be released to such Sonus Partner. The parties acknowledge and agree that at no time after the shipment of Product from Abbott Laboratories manufacturing facility * and during the transport, holding and release of the Product by Abbott pursuant to this Section 6(a) shall Abbott have title to, or any ownership interest or risk of loss in, such Product.

(b) Upon the request of Sonus, Abbott shall assist Sonus in connection with quality assurance release testing of the Product intended for sale in the EU, by conducting such testing in Abbott's laboratory facility * and by providing the results of such testing to Sonus and/or Sonus Partners in the EU (as Sonus may direct), and by determining in its reasonable discretion whether such Product is acceptable for release based upon such test results; and provided further that Abbott's obligations under this Paragraph 6(b) shall cease as of the earlier of (i) the date upon which Abbott employee(s) are no longer designated as "responsible persons" in connection with the Product in the EU and/or in EU member states, or (ii) the end of the three-year period applicable to this Paragraph 6.

(c) Abbott shall assist Sonus in connection with the transition of regulatory activities for the Product, by:

* Confidential portions omitted and filed separately with the Commission.

(i) convening, within thirty (30) days of the date of this letter, a meeting with Sonus to review the status of all pending regulatory activities regarding the Product in the Territory in which Abbott is involved as of the date of this letter and to hand off responsibility for such activities to Sonus (including but not limited to *;

(ii) providing advice to Sonus in connection with Sonus's taking over such activities; and

(iii) continuing such activities as are legally required by virtue of the designation of certain Abbott employees within the EU, as of the date of this letter, as "responsible persons" in connection with the Product in the EU and/ or in EU member states.

7. In consideration for the obligations undertaken by Abbott pursuant to this letter, and in partial recognition of the value added to the Product by virtue of Abbott's performance under the International Agreement, Sonus shall make the following payments to Abbott:

(a)

(i) If Sonus requests and Abbott provides services pursuant to section 6 above, then in consideration for the provision by Abbott of such services, Sonus shall pay to Abbott a fee for services equal to *. If Sonus requests, Abbott shall provide Sonus with an estimate of the costs prior to providing services and shall promptly advise Sonus of any material variance from the estimate.

(ii) Abbott shall invoice Sonus for Abbott's services (and, if applicable, for Abbott's cost for engaging additional resources) on a quarterly basis, and Sonus shall make each payment to Abbott within thirty (30) days of Sonus's receipt of such invoice.

(iii) Notwithstanding any provision elsewhere in this letter, Sonus acknowledges and agrees that, since the assistance to be rendered by Abbott pursuant to section 6(c)(iii) above arises from legal requirement, Abbott shall render such assistance, and Sonus shall pay for such assistance as provided in this section 7(a), regardless of whether Sonus specifically requests such assistance, until such time as Sonus removes the designation of Abbott and Abbott's employees as "responsible persons" in connection with the Product in the EU and in EU member states pursuant to section 9 below.

(b) (i) Regardless of whether Sonus requests and Abbott provides services pursuant to section 6 above, for a period commencing on the date of this letter
("Profit Sharing Commencement Date") and ending on the later of (i) five (5) years from the Profit Sharing Commencement Date, or (ii) the date Abbott should cease co-marketing SonoGen (as defined in Paragraph 10 below) in the event Abbott exercises its option to co-market as provided in Paragraph 10 below, Sonus shall pay to Abbott twenty-one percent (21%) of Sonus Net Profit on Sonus and Sonus Partner sales of the Product in the Territory for so long as that certain Agreement dated May

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14, 1996 between Sonus and Abbott Laboratories, as amended on January 31, 1999 by that certain First Amendment to Agreement (collectively, the "HPD Agreement") is in full force and effect under the terms currently set forth therein. In the event that the terms of the HPD Agreement as currently set forth therein should be modified or amended in any material respect which is financially adverse to Sonus, Abbott and Sonus agree to renegotiate, in good faith, a reduction of the rate of the Abbott Profit Split set forth above to reflect the changed nature of the HPD Agreement resulting from such modification or amendment. In the event the parties are unable to agree upon the reduction in the Abbott Profit Split within thirty (30) days of the commencement of negotiations, the matter shall be resolved by the Alternative Dispute Resolution ("ADR") procedure as provided in
Section 14 below, provided that in no event shall Abbott be entitled to the Abbott Profit Split if the HPD Agreement is cancelled or rescinded by Abbott. In the event that any reduction to the Abbott Profit Split becomes necessary under this Section 7(b), the twenty-one percent (21%) Abbott Profit Split shall continue to be applicable until the date on which the parties agree as to the reduced Abbott Profit Split or the date on which the ADR neutral has issued his or her final decision determining such reduced Abbott Profit Split, whichever occurs sooner. As used herein Sonus Net Profit shall mean the net revenues received by Sonus from sales of the Product in the Territory determined in accordance with generally accepted accounting principles (including revenues received by Sonus from Sonus Partners relating to the sale of the Product in the Territory), net of sales, use, value-added or other similar taxes, transportation, shipping or delivery charges, and discounts actually granted, and less direct expenses associated with the manufacturing, marketing, sale and distribution of the Product, including without limitation any fees payable to Abbott under paragraph 7(a) above. Anything herein to the contrary notwithstanding, the obligations of Sonus to make payments to Abbott under this Paragraph 7(b) shall terminate in the event Abbott or its Affiliates and/or third party agents or representatives should market or sell a competing product in the Territory. For the purpose of this Paragraph 7(b), a "competing product" means an ultrasound contrast agent for intravenous injection.

The following examples are provided by way of illustration only:

Scenario #1 (Abbott performs services requested by Sonus; current HPD Agreement in effect)

*

Scenario #2 (Abbott does not perform services; current HPD Agreement in effect)

*

* Confidential portions omitted and filed separately with the Commission.

*

Scenario #3 (Abbott performs services requested by Sonus; current HPD Agreement in effect, Sonus Partners pay royalties)

*

(ii) Sonus shall pay the Abbott Profit Split to Abbott on a quarterly basis, and shall make each payment to Abbott within thirty (30) days after the end of each calendar quarter in which any Sonus Partner makes any sales of the Product in the Territory.

(iii) At the same time as Sonus makes each Abbott Profit Split payment to Abbott, Sonus shall provide Abbott with a report setting forth the calculation of the Abbott Profit Split for the calendar quarter in question, showing: the aggregate net revenues of Sonus, in the Territory; Sonus's aggregate direct costs, Abbott's aggregate fees for services (if any), Sonus's aggregate payment(s) to Sonus Partners (net of any rebate received by Sonus from Sonus Partners), and Sonus Net Profit. The net revenues of Sonus shall be translated from local currency into United States dollars at the average exchange rate published in International Financial Statistics by the International Monetary Fund for the month ending in the calendar quarter covered in the report.

(c) Sonus shall pay to Abbott fifty percent (50%) of any prepaid royalties or other upfront, fees or consideration which are paid by Sonus Partners to Sonus upon or in connection with the initiation of the relationship and/ or any other cash payments received by Sonus during the term of the agreement with any Sonus Partner which are based upon the occurrence of milestones or events and which are not in the nature of recurring royalties based upon the sales or profits from sales of the Product by Sonus Partners in the Territory, excluding any payments for equity of Sonus or which are in the nature of payments or reimbursement for Sonus's actual cost plus a reasonable markup for research and development, including without limitation, clinical studies, performed or directed by Sonus for the benefit of such Sonus Partner (the "Sonus Partner Fees"). Any amounts received by Sonus which are paid by Sonus Partners but which are not Sonus Partner Fees, shall nonetheless constitute revenue of Sonus if appropriate under generally accepted accounting principles for the purpose of determining Sonus Net Profit under Paragraph 7(b) above. Sonus shall be obligated to make payments under this Paragraph 7(c) during the same period Sonus is obligated to make payments to Abbott under Paragraph 7(b) above. Payments of the percentage of Sonus Partner Fees shall be made within thirty (30) days after the end of the calendar quarter in which Sonus receives each such Sonus Partner Fees from Sonus Partners. One half of the amounts paid by Sonus to Abbott under this Paragraph 7(c) shall be applied as a credit against any obligation of Sonus to make payments to Abbott under Paragraph 7(b) above.

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8. (a) All payments made by Sonus to Abbott pursuant to this letter shall be in United States dollars by wire transfer. Abbott shall provide Sonus with all necessary wire transfer instructions and information.

(b) If any payment by Sonus is more than 30 days overdue, then Sonus shall also pay to Abbott interest on the overdue payment, running from the date on which payment was due, at the United States prime rate of interest then prevailing as published in the Wall Street Journal (Midwest Edition).

(c) Where any sum due to be paid to Abbott hereunder is subject to any withholding or similar tax, the parties shall use their commercially reasonable best efforts to do all such acts and things and to sign all such documents as will enable them to take advantage of any applicable double taxation agreement or treaty. In the event there is no applicable double taxation agreement or treaty, or if an applicable double taxation agreement or treaty reduces but does not eliminate such withholding or similar tax, Sonus shall pay such withholding or similar tax to the appropriate government authority, deduct the amount paid from the amount due Abbott and secure and send to Abbott the best available evidence of such payment.

(d) Sonus shall keep complete copies of all agreements with Sonus Partners and all records relating to the payments made and/ or owing to Abbott pursuant to this letter, and to the calculation of such payments, and shall maintain copies of such agreements and such records for a period of four (4) years after the sales period to which such records relate. During this period, copies of such agreements and such records shall be open to inspection upon reasonable written notice by Abbott to Sonus. Such inspection shall be performed by an independent certified public accountant, selected by Abbott and approved by Sonus (such approval not to be unreasonably withheld). Abbott shall bear the cost of such inspection, except that if an inspection reveals that payments to Abbott have been understated by five percent (5%) or more, and if the understatement is greater than $25,000, Sonus shall pay the cost of such inspection, the understated amount, and interest on the understated amount running from the date on which the payment was originally due at United States prime rate of interest then prevailing as published in the Wall Street Journal (Midwest Edition). Any independent certified public accountant engaged by Abbott shall for an inspection hereunder shall sign a confidentiality agreement prior to any audit and then shall have the right to examine the agreements and records kept pursuant to this subsection 8(d) and report findings (but not disclosure of the specific terms of the agreements or the underlying data) of the examination to Abbott as is necessary to evidence that the records were or were not maintained and used in accordance with this section 8(d) and to evidence that the calculation of the payments to be made and/or owing to Abbott pursuant to this letter was or was not made in accordance with the terms of this letter. A copy of any report provided to Abbott by the independent certified public accountant hereunder shall be given concurrently to Sonus.

(e) Sonus represents and warrants to Abbott that: (i) any and all agreements between Sonus and Sonus Partners in connection with the Product shall be entered into in good faith with terms and conditions negotiated at arms' length and not in any way structured, written or otherwise devised so as to avoid any part or all of Sonus's obligations to pay Abbott pursuant to section 7 above

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(f) Sonus acknowledges and agrees that Sonus shall bear all responsibility and liability with respect to any and all third parties in connection with any services provided by Abbott to Sonus and/ or Sonus Partners under this letter, subject only to paragraph 1 above.

9. Notwithstanding any provision elsewhere in this letter, Sonus shall use its commercially reasonable best efforts, as expeditiously as possible, to replace Abbott's employees in the EU as designated "responsible persons" in connection with the Product in the EU and in EU member states, with Sonus employees, Sonus Partners, or any other Sonus representative, agent or contractor (at Sonus's sole discretion as to the specific choice of replacement individuals) ("Sonus Replacements"), including but not limited to the prompt submission of any and all such applications, notifications, variations and other materials or information required by the relevant EU and EU member state authorities in order to end any legal responsibility on the part of Abbott and/ or Abbott's employees in the EU as "responsible persons" in connection with the Product in the EU and in EU member states. Abbott shall fully cooperate with Sonus in such transition and shall provide Sonus with such assistance as Sonus may reasonably request in connection therewith, pursuant to section 6(c)(iii) above. On a country by country basis, Abbott's obligations under section 6(c)(iii) above shall cease as Abbott's employees in the EU are removed as "responsible persons" in connection with the Product in the EU and in EU member states. Sonus acknowledges and agrees that, if Sonus has not replaced all of Abbott's employees in the EU who are such "responsible persons" as of the date of this letter with Sonus Replacements, by at least twelve (12) months prior to the end of the three (3) year period applicable to section 6 above, then Sonus shall, no later than eleven (11) months prior to the end of such three (3) year period, submit any and all such applications, notifications, variations and other materials or information required by the relevant EU and EU member state authorities, in order to end any legal responsibility on the part of Abbott and Abbott's employees in the EU and in EU member states as "responsible persons" in connection with the Product in the EU and in EU member states, regardless of whether or not any Sonus Replacement(s) have been identified or submitted at that time.

10. Sonus hereby grants to Abbott the option to co-market that product identified by Sonus as "QW7437" and also known as SonoGen(R), including all improvements thereon ("SonoGen"), in the Territory, subject to the terms and conditions of a separate agreement to be negotiated in good faith by the parties, which terms shall be no less, nor no more, favorable in any material respect from the terms of any agreement between Sonus and any third party in the applicable country included within the Territory, or, if there is no such agreement in the relevant country in the Territory, on terms and conditions substantially similar to those of the International Agreement. Abbott shall have the right to exercise this option for a period (the "Option Period") commencing on the date of this letter and ending on the earlier to occur of (i) five (5) years from the date of this letter, or (ii) the date the obligations of Abbott under Section 11 below should terminate. The option to co-market may be exercised only one time for the entire Territory. Abbott may irrevocably terminate its option to co-market upon notice to Sonus at any time after the date of this letter in which event the rights of Abbott under this Paragraph 10 and the obligations of Abbott under Paragraph 11 shall terminate. Sonus shall not grant any rights to market, distribute or sell SonoGen in the Territory to more than one (1) other third party in a given country in the Territory and shall not, by itself or through any Sonus Affiliate, market, distribute or sell SonoGen in a given country in the Territory if such action by Sonus would cause there to be more than two entities (one of which being Abbott) marketing, distributing or selling SonoGen in such country in the Territory at the same time.

* Confidential portions omitted and filed separately with the Commission.

11. For a period commencing on the date of this letter and continuing until the later to occur of: (i) the end of the Option Period or (ii) the end of the period of time during which Abbott is exercising its co-marketing rights as provided in paragraph 10 above, Abbott shall not (nor shall Abbott cause its Affiliates and/ or third party agents or representatives to) market or sell a competing product in the Territory. The above notwithstanding, the obligations of Abbott under this paragraph 11 shall terminate at such date on which Abbott notifies Sonus that it has terminated its option to co-market under paragraph 10 above or the expiration of the Option Period. For the purposes of this section 11, a "competing product" means an ultrasound contrast agent for intravenous injection.

12. Either party may terminate the rights and obligations of sections 1 through 18 of this letter (not including the rescission of the International Agreement) in accordance with the following provisions (in addition to any other rights and remedies which may be available to that party):

(a) By notice by one party to the other party upon (i) the insolvency of the other party, or the appointment of a receiver by the other party for all or any substantial part of its properties, provided that such receiver is not discharged within sixty (60) days of his/ her appointment; (ii) the adjudication of the other party as a bankrupt; (iii) the admission by the other party in writing of its inability generally to pay its debts as they become due; (iv) the execution by the other party of an assignment for the benefit of its creditors; or (v) the filing by the other party of a petition to be adjudged a bankrupt, or a petition or answer admitting the material allegations of a petition filed against the other party in any bankruptcy proceeding, or the act of the other party in instituting or voluntarily being or becoming a party to any other judicial proceeding intended to effect a discharge of the debts of the other party, in whole or in substantial part.

(b) By ninety (90) days notice by one party to the other party of the other party's breach of a material provision of this letter, provided that the other party has failed to remedy such breach to the notifying party's reasonable satisfaction within such ninety (90) day period.

13. Neither party may assign or transfer its obligations under this letter, by operation of law or otherwise, except that either party may assign this letter to any of its Affiliates, or to any successor by merger or sale of substantially all of its business unit to which this letter relates without the consent of the other party. This letter and the rights and obligations hereof shall inure to the benefit of and be binding upon the parties hereto and their permitted assigns.

14. Any dispute that arises in connection with this letter shall first be presented to the respective presidents of Abbott and of Sonus, or their designees, for resolution. If no resolution is reached, then such dispute shall be resolved by binding ADR in the manner described in Appendix 14 attached hereto and made a part hereof.

15. The relationship of the parties under this letter is that of independent contractors. Nothing in this letter shall be construed or is intended so as to constitute the parties as partners, joint venturers, or either party as an agent or employee of the other. Neither party has any express or implied right under this letter to assume or create any obligation on behalf of or in the name of the other, or to bind the other party to any contract, agreement or undertaking with any third party, and no conduct of the parties shall be deemed to infer such right.

* Confidential portions omitted and filed separately with the Commission.

16. This letter sets forth the entire understanding and agreement of the parties with respect to the subject matter hereof and supercedes any and all prior agreements, written and oral, between the parties. No modification of any of the terms of this letter shall be valid, including any course of dealing or usage of trade, unless it is made in writing and signed by both parties. If any term or provision of this letter shall for any reason be held invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other term or provision hereof.

17. No waiver by either party of any default, right or remedy shall be effective unless in writing, nor shall any such waiver operate as a waiver of any other or of the same default, right or remedy respectively, on a future occasion.

18. This letter shall be governed by the laws of the state of Washington, excluding its choice of laws provisions.

If you are in agreement, please sign both originals of this letter and return one fully-executed original to me.

Very truly yours,

/s/ William Dempsey

William Dempsey

ACCEPTED:

SONUS PHARMACEUTICALS, INC.

By: /s/ Michael A. Martino

Title: President and CEO
---

* Confidential portions omitted and filed separately with the Commission.

ALTERNATIVE DISPUTE RESOLUTION

The parties recognize that a bona fide dispute as to certain matters may arise from time to time during the term of this Agreement which relates to either party's right and/or obligations. To have such a dispute resolved by this Alternative Dispute Resolution ("ADR") provision, a party first must send written notice of the dispute to the other party for attempted resolution by good faith negotiations between their respective presidents (or their equivalents) of the affected subsidiaries, divisions, or business units within twenty-eight (28) days after such notice is received (all references to "days" in this ADR provision are to calendar days).

If the matter has not been resolved within twenty-eight (28) days of the notice of dispute, or if the parties fail to meet within such twenty-eight (28) days, either party may initiate an ADR proceeding as provided herein. The parties shall have the right to be represented by counsel in such a proceeding.

1. Initiation of ADR Proceeding. To begin an ADR proceeding, a party shall provide written notice to the other party of the issues to be resolved by ADR. Within fourteen (14) days after its receipt of such notice, the other party may, by written notice to the party initiating the ADR, add additional issues to be resolved within the same ADR.

2. Selection of Neutral. Within twenty-one (21) days following receipt of the original ADR notice, the parties shall select a mutually acceptable neutral to preside in the resolution of any disputes in this ADR proceeding. If the parties are unable to agree on a mutually acceptable neutral within such period, either party may request the President of the CPR Institute for Dispute Resolution ("CPR"), 366 Madison Avenue, 14th Floor, New York, New York 10017, to select a neutral pursuant to the following procedures:

(a) The CPR shall submit to the parties a list of not less than five (5) candidates within fourteen (14) days after receipt of the request, along with a Curriculum Vitae for each candidate. No candidate shall be an employee, director, or shareholder of either party or any of their subsidiaries or affiliates.

(b) Such list shall include a statement of disclosure by each candidate of any circumstances likely to affect his or her impartiality.

(c) Each party shall number the candidates in order of preference (with the number one (1) signifying the greatest preference) and shall deliver the list to the CPR within seven (7) days following receipt of the list of candidates. If a party believes a conflict of interest exists regarding any of the candidates, that party shall provide a written explanation of the conflict to the CPR along with its list showing its order of preference for the candidates. Any party failing to return a list of preferences on tie shall be deemed to have no order of preference.

(d) If the parties collectively have identified fewer than three (3) candidates deemed to have conflict, the CPR immediately shall designate as the neutral the candidate

* Confidential portions omitted and filed separately with the Commission.

for whom the parties collectively have indicated the greatest preference. If a tie should result between two candidates, the CPR may designate either candidate. If the parties collectively have identified three (3) or more candidates deemed to have conflicts, the CPR shall review the explanations regarding the conflicts and, in its sole discretion, may either (i) immediately designate as the neutral the candidate for whom the parties collectively have indicated the greatest preference, or (ii) issue a new list of not less than five
(5) candidates, in which case the procedures set forth in subparagraphs 2(a) - 2(d) shall be repeated.

3. Hearing. No earlier than twenty-eight (28) days or later than fifty six
(56) days after selection, the neutral shall hold a hearing to resolve each of the issues identified by the parties. The ADR proceeding shall take place at a location agreed upon by the parties. If the parties cannot agree, the neutral shall designate a location other than the principal place of business of either party or any of their subsidiaries or affiliates.

4. Exchange of Information Within thirty-five (35) days following receipt of the original ADR notice, each party shall submit the following to the other party and neutral:

(a) a copy of all documents on which such party intends to rely in any oral or written presentation to the neutral; and

(b) a list of any witnesses such party intends to call at the hearing, and a short summary of the anticipated testimony of each witness.

At least fourteen (14) days prior to the hearing, each party shall submit the following to the other party and the neutral:

(c) a proposed ruling on each issue to be resolved, together with a request for a specific damage award or other remedy for each issue. The proposed rulings and remedies shall not contain any recitation of the facts or any legal arguments and shall not exceed one (1) page per issue.

(d) a brief in support of such party's proposed rulings and remedies, provided that the brief shall not exceed twenty (20) pages. This page limitation shall apply regardless of the number of issues raised in the ADR proceeding.

Except as expressly set forth in subparagraphs 4(a) - 4(d), no discovery shall be required or permitted by any means, including depositions, interrogations, request for admissions or production of documents.

5. Conduct of Hearing. The hearing shall be conducted on two (2) consecutive days and shall be governed by the following rules:

* Confidential portions omitted and filed separately with the Commission.

(a) Each party shall be entitled to five (5) hours of hearing time to present its case. The neutral shall determine whether each party has had the five (5) hours to which it is entitled.

(b) Each party shall be entitled, but not required, to make an opening statement to present regular and rebuttal testimony, documents or other evidence, to cross-examine witnesses, and to make a closing argument. Cross-examination of witnesses shall occur immediately after their direct testimony, and cross-examination time shall be charged against the party conducting the cross-examination.

(c) The party initiating the ADR shall begin the hearing and, if it chooses to make an opening statement, shall address not only issues it raised but also any issues raised by the responding party. The responding party, if it chooses to make an opening statement, also shall address all issues raised in the ADR. Thereafter, the presentation of regular and rebuttal testimony and documents, other evidence, and closing arguments shall proceed in the same sequence.

(d) Except when testifying, witnesses shall be excluded from the hearing until closing arguments.

(e) Settlement negotiations, including any statements made therein, shall not be admissible under any circumstances. Affidavits prepared for purposes of the ADR hearing also shall not be admissible. As to all other matters, the neutral shall have sole discretion regarding the admissibility of any evidence.

6. Post-Hearing Brief. Within seven (7) days following completion of the hearing, each party may submit to the other party and the neutral a post-hearing brief in support of its proposed rulings and remedies, provided that such brief shall not contain or discuss any new evidence and shall not exceed ten (10) pages. This page limitation shall apply regardless of the number of issues raised in the ADR proceeding.

Within eleven (11) days following completion of the hearing, each party may submit to the other party and the neutral a post-hearing rebuttal brief, responding to the matters raised in the other party's post hearing brief, provided that such rebuttal brief shall only respond to matters raised in the other party's post-hearing brief, shall not contain or discuss any new evidence, and shall not exceed five (5) pages.

7. Ruling. The neutral shall rule on each disputed issue within seventeen (17) days following completion of the hearing. Such ruling shall adopt in its entirety the proposed rulings and remedy of one of the parties on each disputed issue but may adopt one party's proposed rulings and remedies on some issues and the other party's proposed rulings and remedies on other issues. The neutral shall not issue any written opinion or otherwise explain the basis of the ruling.

* Confidential portions omitted and filed separately with the Commission.

8. Neutral's Fees. The neutral shall be paid a reasonable fee plus expenses. These fees and expenses, along with the reasonable legal fees and expenses of the prevailing party (including all expert witness fees and expenses), the fees and expenses of a court reporter, and any expenses for a hearing room, shall be paid as follows:

(a) If the neutral rules in favor of one party on all disputed issues in the ADR, the losing party shall pay 100% of such fees and expenses.

(b) If the neutral rules in favor of one party on some issues and the other party on other issues, the neutral shall issue with the rulings a written determination as to how such fees and expenses shall be allocated between the parties. The neutral shall allocate fees and expenses in a way that bears a reasonable relationship to the outcome of the ADR, with the party prevailing on more issues, or on issues of greater value or gravity, recovering a relatively larger share of its legal fees and expenses.

9. Binding Ruling. The rulings of the neutral and the allocation of fees and expenses shall be binding, non-reviewable, and non-appealable, and may be entered as a final judgement in any court having jurisdiction.

10. Confidentiality. Except as provided in Section 9 above or as required by law, the existence of the dispute, any settlement negotiations, the ADR hearing, any submissions (including exhibits, testimony, proposed rulings, and briefs), and rulings shall be deemed Confidential Information. The neutral shall have the authority to impose sanctions for unauthorized use or disclosure of Confidential Information.

* Confidential portions omitted and filed separately with the Commission.

ARTICLE 5

PERIOD TYPE	3 MOS
FISCAL YEAR END	DEC 31 1999
PERIOD START	JUL 1 1999
PERIOD END	SEP 30 1999
CASH	7,658,072
SECURITIES	7,490,663
RECEIVABLES	5,000,000
ALLOWANCES	0
INVENTORY	0
CURRENT ASSETS	165,499
PP&E	4,035,973
DEPRECIATION	(3,061,399)
TOTAL ASSETS	21,288,809
CURRENT LIABILITIES	9,236,195
BONDS	0
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	37,131,042
OTHER SE	(25,078,428)
TOTAL LIABILITY AND EQUITY	21,288,809
SALES	0
TOTAL REVENUES	10,000,000
CGS	0
TOTAL COSTS	3,130,807
OTHER EXPENSES	0
LOSS PROVISION	0
INTEREST EXPENSE	(20,335)
INCOME PRETAX	6,912,329
INCOME TAX	0
INCOME CONTINUING	6,912,329
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	6,912,329
EPS BASIC	.77
EPS DILUTED	.76

End of Filing

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