2010
ANNUAL
REPORT

Accelerating Opportunity

InSite Vision is committed to advancing new and superior ophthalmic products for unmet eye care needs.

InSite Vision has successfully developed two commercially-available products for the treatment of bacterial eye infections and continues to pioneer new ophthalmic therapeutics, with multiple clinical-stage candidates intended for the treatment of eye inflammation, infection, post-operative pain, dry eye disease and other eye diseases.

The company's product portfolio utilizes InSite Vision's proven DuraSite® drug delivery platform. The DuraSite bioadhesive polymer core technology extends the duration of drug retention on the surface of the eye, thereby reducing frequency of treatment and improving the efficacy of topically-delivered drugs. InSite's commercial products include AzaSite® (azithromycin ophthalmic solution) 1%, marketed in the U.S. by Inspire Pharmaceuticals, and Besivance™ (besifloxacin ophthalmic suspension) 0.6%, marketed by Bausch & Lomb and Pfizer Inc., both approved for the treatment of bacterial conjunctivitis. On April 5, 2011, Merck announced that they have entered into a definitive agreement to acquire Inspire Pharmaceuticals.

InSite Vision's pipeline of clinical-stage products includes two Phase 3 clinical candidates for the treatment of blepharitis: AzaSite Plus™ (ISV-502), a combination of azithromycin and dexamethasone in DuraSite, and DexaSite™ (ISV-305), which combines dexamethasone in DuraSite. A third Phase 3 clinical candidate, ISV-303 (0.075% bromfenac in DuraSite), is being developed for the once-daily treatment of pain and inflammation associated with ocular surgery. InSite's clinical-stage pipeline also includes ISV-101, a lower dose formulation of bromfenac with DuraSite for the treatment of dry eye disease.

Rich Pipeline

Building for the Future

The InSite Vision portfolio includes marketed products and products in late-stage clinical development.

	PRECLINICAL	PHASE I	PHASE II	PHASE III	FILED	MARKETED
LICENSED						
AzaSite® (azithromycin ophthalmic solution) 1% **Bacterial conjunctivitis** Marketed by Inspire Pharmaceuticals, Inc.						●
Besivance™ (besifloxacin opthalmic suspension) 0.6% **Bacterial conjunctivitis** Marketed by Bausch & Lomb and their partner Pfizer Inc.						●
IN DEVELOPMENT						
AzaSite Plus™ (ISV-502) (azithromycin 1% & dexamethasone 0.1% in DuraSite®) **Blepharitis/Lid margin disease**				●		
DexaSite™ (ISV-305) (dexamethasone 0.1% in DuraSite®) **Non-bacterial blepharitis**				●		
ISV-303 (bromfenac 0.075% in DuraSite®) **Post-operative pain & inflammation**				●		
ISV-101 (lower dose bromfenac in DuraSite®) **Dry eye disease**		●				

April 19, 2011

Dear Shareholders

We believe that 2011 will be a transformational year for InSite Vision – due to the great strides made in 2010 by our dedicated team to solidify and advance a proprietary pipeline of product candidates based on InSite's DuraSite® drug delivery platform.

Positioned for Success

Having joined the management team in December 2010, I continue to be enthusiastic about InSite's future prospects and strong core assets, including our validated DuraSite technology platform that has produced two successful therapeutic products that are in the marketplace and benefitting patients today. The DuraSite platform has been further leveraged to create a deep pipeline of ophthalmic therapeutics, ranging from Phase 3 clinical candidates to preclinical compounds, each targeting important eye care needs and significant market opportunities. I believe InSite Vision has a great team in place and I continue to be impressed by my colleagues' commitment to advancing meaningful new ophthalmic pharmaceuticals.

Last year, we promised that 2010 would be one of visible momentum as we built value in our pipeline assets. We successfully executed on those objectives, and today I am pleased to describe substantial progress across our business.

Moving Forward

Among the most important objectives has been to build a close collaborative relationship with the U.S. Food and Drug Administration (FDA) as we endeavor to obtain a Special Protocol Assessment (SPA) agreement for a Phase 3 clinical trial evaluating both AzaSite Plus™ (ISV-502) and DexaSite™ (ISV-305) for the treatment of blepharitis. Blepharitis is a chronic and complex condition characterized by inflammation of the eyelid. Based on our prior clinical studies of AzaSite Plus and DexaSite, we know that each of these compounds is highly active and possesses an established safety profile. Through this lengthy but important SPA agreement process, we made significant headway in establishing well-defined endpoints for a Phase 3 trial designed to evaluate both of these promising compounds in a single clinical study, which we believe we can obtain.

In addition to our efforts to advance two effective treatments for blepharitis, a third product candidate for the treatment of post-surgical pain and inflammation, ISV-303, is now poised for Phase 3 development. We announced top-line results in March 2011 from our Phase 1/2 clinical trial of ISV-303 in patients following cataract surgery. These data indicate that ISV-303 administered once-daily is an active and efficacious ophthalmic NSAID. We believe the statistically significant evidence of ISV-303's potent activity over vehicle indicates a clear regulatory pathway, and we plan to work closely with the FDA on the design of a Phase 3 clinical trial.

Finally, we advanced another novel product candidate toward the clinic, ISV-101, and completed the filing of an Investigational New Drug Application (IND) with the FDA in January 2011. ISV-101 is being developed for the treatment of dry eye disease. We anticipate initiating a Phase 1/2 clinical trial later this year to evaluate the safety and efficacy of ISV-101 when administered twice daily.

Managing our Resources

As we drive our pipeline candidates forward, we remain focused on the careful management of our resources. In 2010, we saw our total royalty revenues increase by approximately 39 percent driven by royalties from product sales of AzaSite® (marketed by Inspire Pharmaceuticals) and Besivance™ (marketed by Bausch & Lomb and Pfizer Inc.). Of note, AzaSite royalties for the last half of 2010 exceeded both the interest payments due on the AzaSite bonds issued by our subsidiary in 2008 as well as our Pfizer royalty payments. Per the terms of our agreement, we are entitled to receive increasing minimum royalty payments over the next three years.

In spite of increased product development activity, research and development expenses for 2010 remained roughly even with 2009 levels and we successfully reduced 2010 general and administrative expenses from those in 2009.

Building for the Future

Our strategy is to steadily advance our products, and in doing so we believe we will naturally create opportunities to build value for our shareholders.

We believe we are well positioned among our ophthalmic therapeutic peers with a number of very attractive product opportunities suitable for significant commercial development agreements. We will carefully evaluate all potential partnering opportunities to ensure that they are appropriately valued. If we feel that we are not seeing the right terms, we plan to proceed with our product development efforts independently – continuing to build value in each of our programs.

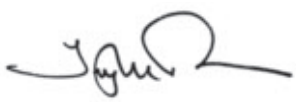
Today, as a company with three Phase 3 clinical candidates, a proven technology platform and increasing revenues, I continue to believe that InSite is undervalued. To that end, we are steadily increasing our financial community outreach efforts to tell the InSite story. I believe our achievements and our steady execution will be of compelling interest to our current investors and those new to the InSite Vision story. As such, one of our objectives for 2011 will be to rejoin a major stock exchange. Doing so would allow us to broaden our institutional base and attract investors and analysts who may not otherwise be able to support our future success.

With a strong foundation for growth in place, a solid strategy and an unwavering focus on moving our company forward, the coming year should be one of important progress for InSite Vision.

I look forward to keeping you updated on our accomplishments.

Thank you for your support.

Sincerely,



Timothy Ruane
Chief Executive Officer

Form 10-K

2010 Annual Report

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

FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2010

OR

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

Commission file number: 0-22332

INSITE VISION INCORPORATED
(Exact name of registrant as specified in its charter)

Delaware	**94-3015807**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
965 Atlantic Avenue, Alameda CA	**94501**
(Address of principal executive offices)	**(Zip Code)**

(510)-865-8800
(Registrant's telephone number, including area code)

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

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

Title of each class	Name of each exchange on which registered
Common Stock, $0.01 par value per share	OTC Bulletin Board

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

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

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

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

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

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

Large accelerated filer ☐ Accelerated filer ☐
Non-accelerated filer ☐ Smaller reporting company ☒

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

The aggregate market value of registrant's Common Stock, $0.01 par value, held by non-affiliates of the Registrant as of June 30, 2010 was approximately $25,717,407 (based upon the closing sale price of the Common Stock on the last business day of the registrant's most recently completed second fiscal quarter). Shares of Common Stock held by each officer and director and by each person who owns 5% or more of the Common Stock have been excluded from such calculation as such persons may be deemed affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

Number of shares of Common Stock, $0.01 par value, outstanding as of February 28, 2011: 94,822,593.

Documents Incorporated By Reference

Listed below is the document incorporated by reference and the part of the Form 10-K into which the document is incorporated:

Portions of the Registrant's definitive proxy statement (the "Proxy Statement") for the Registrant's 2011 annual meeting of stockholders (the "Annual Meeting") are incorporated by reference in Part III of this Annual Report on Form 10-K to the extent stated herein.

ANNUAL REPORT ON FORM 10-K
FOR THE YEAR ENDED DECEMBER 31, 2010

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Except for the historical information contained herein, the discussion in this Annual Report on Form 10-K contains certain forward-looking statements that involve risks and uncertainties, such as statements of our plans, beliefs, objectives, expectations and intentions. Our actual results could differ materially from those discussed herein. Factors that could cause or contribute to such differences include those discussed below in "Risk Factors," as well as those discussed elsewhere herein. The cautionary statements made in this document should be read as applicable to all related forward-looking statements wherever they appear in this document. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

PART I

Item 1. Business

THE COMPANY

InSite Vision Incorporated ("InSite" or the "Company") is an ophthalmic product development company advancing ophthalmic pharmaceutical products to address unmet eye care needs. Our current portfolio of products is based on our proprietary DuraSite® drug delivery technology.

Our DuraSite® sustained drug delivery technology is a proven synthetic polymer-based formulation designed to extend the residence time of a drug relative to conventional topical therapies. It enables topical delivery of a drug as a solution, gel or suspension and can be customized for delivering a wide variety of drug candidates. We have focused our research and development and commercial support efforts on the following topical products formulated with our DuraSite® drug delivery technology. We may also utilize our DuraSite technology platform for the formulation of new ocular product candidates using either non-proprietary drugs or compounds originally developed by others for non-ophthalmic indications.

- AzaSite® (azithromycin ophthalmic solution) 1% is a DuraSite formulation of azithromycin, a broad spectrum ocular antibiotic approved by the United States Food and Drug Administration ("FDA") in April 2007 to treat bacterial conjunctivitis (pink eye). It was launched in the United States by Inspire Pharmaceuticals in August 2007. Additional indications are being pursued by Inspire Pharmaceuticals for this product. The key advantages are a significantly reduced dosing regimen leading to better compliance and outcome, with a broad spectrum antibiotic, and a lowered probability of bacterial resistance based on high tissue concentration.
- Besivance™ (besifloxacin ophthalmic suspension) 0.6% is a DuraSite formulation of besifloxacin, a broad spectrum ocular antibiotic approved by the FDA in May 2009 to treat bacterial conjunctivitis (pink eye). An advantage of Besivance is a faster rate of resolution of the infection that may reduce the duration of the illness and reduce the chances of infecting others. Besivance was developed by Bausch & Lomb and launched in the United States in the second half of 2009.
- AzaSite Plus™ (ISV-502) is a fixed combination of azithromycin and dexamethasone in DuraSite for the treatment of ocular inflammation and infection (blepharitis and/or blepharoconjunctivitis) for which there is no FDA-approved indicated treatment; we completed the first Phase 3 trial in November 2008. AzaSite Plus was very well tolerated. However, the trial did not achieve its primary endpoint as defined by the protocol. We discussed the results of this trial with the FDA and determined a development plan for this product candidate. We are pursuing a Special Protocol Assessment ("SPA") for the next Phase 3 clinical trial for this product candidate. An SPA is a declaration from the FDA that a Phase 3 trial's design, clinical endpoints and statistical analysis are acceptable for regulatory approval.
- DexaSite™ (ISV-305) is a DuraSite formulation of dexamethasone in development for the treatment of ocular inflammation. We have met with the FDA to discuss the development pathway for this product candidate. We are pursuing an SPA for the next Phase 3 clinical trial for this product candidate.

- ISV-303 is a DuraSite formulation of bromfenac in development for the treatment of post-operative inflammation and eye pain. We initiated a Phase 1/2 clinical trial for this product candidate in August 2010 and completed patient enrollment in December 2010. We expect to have top-line results from this study in the first half of 2011. In addition, we anticipate an additional Phase 2 clinical trial to investigate the pharmacokinetics of ISV-303 in humans.
- ISV-101 is a DuraSite formulation with a low concentration of bromfenac for the treatment of dry eye disease. We filed an Investigational New Drug Application (IND) for this product candidate in the first quarter of 2011. We anticipate a Phase 1/2 clinical trial for this product candidate.

Business Strategy.

Our business strategy consists of the following:

1. **Develop our pipeline of ocular product candidates.** We identify new product candidates that consist of proven drugs that can be improved by formulation in DuraSite, which substantially reduces the clinical risk in these product candidates. We plan to conduct preclinical and clinical testing of our portfolio product candidates.

2. **Monetize our product candidates.** At the appropriate time, we seek to partner with larger pharmaceutical companies to complete the clinical development, manufacture and marketing of these products. Partnering agreements generally include upfront and milestone payments, as well as on-going royalty payments upon commercialization, for the Company.

Corporate Information. Our principal executive offices are located at 965 Atlantic Avenue, Alameda, California 94501. Our telephone number is (510) 865-8800. We were incorporated in 1986 as a California corporation and reincorporated in Delaware in 1987. We make our periodic and current reports available, free of charge, through our website (http:///www.insitevision.com) under "Investor Relations—SEC Filings" as soon as reasonably practicable after such material is electronically filed with the Securities and Exchange Commission. Additionally, copies of materials filed by us with the SEC may be accessed at the SEC's Public Reference Room at 100 F Street NE, Washington D.C. or at the SEC's website at http://www.sec.gov. For information about the SEC's Public Reference Room, the public may contact 1-800-SEC-0330.

Ophthalmic Anti-Infective Market

Today, eye infections are routinely treated with topical antibiotics as well as antibiotic/corticosteroid fixed combination products. The ocular anti-infective market represented global sales of approximately $2.0 billion in 2010 and comprises two separate product segments:

- Ocular antibiotic products
- Ocular antibiotic/corticosteroid fixed combination products

We are developing differentiated topical products to treat eye and eye-lid infections. Some of these infections are either under-treated or do not have an FDA-approved product indication. These infections can be both acute and chronic. Our goal is to provide effective and differentiated therapeutics for the treatment of acute and chronic ocular infection and inflammation. There are two general areas where our topical ocular anti-infective products have been utilized by eye care physicians, or where we believe our product candidates may be well-suited to improving patient care:

- Eye Infections.
    - *Acute bacterial conjunctivitis* (pink eye) is a common condition experienced by most people at some point in their lives, but is especially prevalent among children. The conjunctiva is the transparent lining on the inside of the eyelids. In bacterial conjunctivitis, bacteria infects this

lining, and the white part of the eye may look pink from the inflammation. As it is an extremely contagious condition, immediate treatment is recommended. Our developed ocular antibiotics, AzaSite and Besivance, are targeted at treating this disease with significantly lower dosing than competing products.

- *Eye-lid infections*.
  - *Blepharitis* (also known as lid margin disease) is an inflammation of the eyelids, particularly the eyelid margins where the eyelashes grow. It is a common disorder, particularly among the elderly, that may be caused by bacterial growth, viral infection, allergies, environmental conditions or systemic disease. An eyelid with blepharitis may become itchy and appear red and swollen with scaly, greasy debris along the lid margin. Blepharitis can be a chronic condition that is difficult to treat. There are no approved pharmaceutical products for the treatment of blepharitis. Patients are typically advised to use lid scrubs, hot compresses, lid massage, antibiotics, corticosteroids and fixed-combination products. We are advancing two novel ophthalmic products to address the signs and symptoms of blepharitis, AzaSite Plus, a topical anti-bacterial and anti-inflammatory product, and DexaSite, a corticosteroid anti-inflammatory agent.
  - *Blepharoconjunctivitis* occurs when conjunctivitis accompanies blepharitis, as it frequently does. A unilateral or bilateral conjunctivitis that persists for four or more weeks is considered chronic. There is a considerable overlap of symptoms of all types of blepharitis. It frequently leads to associated ocular surface inflammation, including conjunctivitis, function tear deficiency and keratitis (an inflammation of the cornea which can develop into corneal ulcers). Blepharoconjunctivitis is a disease with no approved drug therapy indicated for the relief of its chronic symptoms. Typical treatment include eye hygiene using lid scrubs, topical and/or systemic antibiotics and topical corticosteroids.

Ocular Inflammation and Pain Market

We are developing novel ophthalmic therapeutics for the treatment of conditions associated with ocular inflammation. These efforts are initially focused on two indications, post-operative inflammation and pain, and dry eye disease.

- *Post-Operative Ocular Inflammation and Pain* is typically treated using non-steroidal anti-inflammatories (NSAIDs). An estimated 60 percent of ophthalmic surgeons deploy topical NSAIDs before and after cataract and other procedures to address patient pain and prevent serious complications, such as cystoid macular edema. Cystoid macular edema is a serious post-surgical complication that occurs when inflammation and swelling develop in the center of the retina. It is the most common cause of decreased vision following cataract surgery. Cataract surgery is one of the most frequent surgical procedures conducted in the United States. It is estimated that as the population in the U.S. ages, the market for ocular NSAIDs that are efficacious and easy for patients to use will grow 7.1 percent between 2007 and 2014. Our ISV-303 product candidate is intended to provide superior tissue penetration of drug to the eye with convenient twice-daily dosing.
- *Dry Eye Disease* occurs when the ocular surface and/or tear film is compromised. While causes of dry eye may vary, it is frequently associated with inflammation of the surface of the eye, the lacrimal gland, or the conjunctiva. A potentially chronic condition that can occur at any age, dry eye disease is most prevalent among the elderly. Symptoms of dry eye disease include a scratchy feeling as if something is in the eye, stinging or burning of the eye; episodes of excess tearing that follow periods of very dry sensation; stringy discharge from the eye and pain or redness. According to the National Eye Institute, dry eye disease is estimated to affect five million people age 50 and older in the U.S. alone. The Company has developed a low-dose topical NSAID, known as ISV-101, intended for the treatment of dry eye disease.

Products and Product Candidates

The following table summarizes the current status of our principal products and product candidates in our development pipeline. A more detailed description of each product and product candidate follows the table.

Principal DuraSite Products and Product Candidates
Active Programs

Product	Indications	Anticipated Benefits	Status
AzaSite	Bacterial conjunctivitis (pink eye)	Broad spectrum macrolide antibiotic with reduced dosing frequency	*Approved and launched in US *Approved in Canada
Besivance	Bacterial conjunctivitis (pink eye)	Broad spectrum fluoroquinolone antibiotic with reduced dosing frequency	*Approved and launched in US
AzaSite Plus	Blepharitis	Broad spectrum antibiotic combined with a potent corticosteroid with reduced dosing frequency to treat both inflammation and infection	Phase 3 trial completed
DexaSite	Ocular inflammation	A potent corticosteroid with reduced dosing frequency to treat inflammation	Phase 3 trial completed
ISV-303	Post-Operative inflammation and eye pain	A non-steriodal anti-inflammatory with reduced dosing frequency to treat pain and inflammation	Phase 1/2 clinical trial completed
ISV-101	Dry Eye Disease	A non-steriodal anti-inflammatory to treat dry eye disease	Filed an IND with the FDA

The DuraSite Product Family of Topical Anti-infectives and Product Candidates

AzaSite: Launched commercially in the United States by Inspire Pharmaceuticals in August 2007 for Bacterial Conjunctivitis (pink eye)

We developed a topical formulation of the antibiotic azithromycin to treat bacterial conjunctivitis and other infections of the eye. Bacterial conjunctivitis is a common ocular surface disease characterized by inflammation of the delicate skin and mucosa on the inside of the eyelids. These bacterial infections are contagious and are generally accompanied by irritation, itching, foreign body sensation, watering, mucus discharge and redness. The bacterial form of the disease is generally more common in children than adults.

Azithromycin has a broad spectrum of antibiotic activity and is widely used to treat respiratory and other infections in its oral and parenteral forms. AzaSite is an eye drop of 1% azithromycin formulated to deliver sufficient tissue concentrations over a seven-day dosing period using our proprietary DuraSite technology. The eye drop is designed to enable superior bactericidal activity against common ocular pathogens and even difficult

bacteria such as pseudomonas. We believe the key advantages of AzaSite include its once-a-day dosing after the first two days of treatment and the high and persistent levels of azithromycin achieved in the tissues of the eye. Clinical studies have shown that AzaSite is well tolerated and efficacious. AzaSite was approved by the FDA in April 2007. In August 2007, Inspire Pharmaceuticals commercially launched AzaSite in the United States pursuant to their license from InSite. AzaSite is positioned to compete favorably with the newer fourth generation fluoroquinolones for antibacterial coverage.

Besivance: Launched commercially in the United States by Bausch & Lomb and their partner Pfizer Inc. in second half of 2009 for Bacterial Conjunctivitis (pink eye)

Besivance (besifloxacin ophthalmic suspension 0.6%) is indicated for the treatment of bacterial conjunctivitis in patients one year or older and is marketed by Bausch & Lomb and their partner, Pfizer Inc.

Besivance is the first fluoroquinolone specifically developed for ophthalmic use and is the first and only ophthalmic fluoroquinolone with no previous systemic use. It offers broad-spectrum antibacterial activity, including activity against the strains that are the most common causes of bacterial conjunctivitis.

The FDA approval of Besivance was based on a series of eight clinical trials. These studies were designed to test the efficacy, safety, tolerability, pharmacokinetics and pharmacodynamics with the topical antibacterial. Its efficacy was evaluated in three multi-center, randomized, double-masked trials involving nearly 2,400 patients with a clinical diagnosis of bacterial conjunctivitis. In clinical trials, investigators found that Besivance treatment resulted in a greater proportion of patients experiencing clinical resolution and microbial eradication, when compared to its vehicle.

Besivance was approved by the FDA in May 2009 following a unanimous recommendation by an FDA Advisory Committee in December 2008. The product was launched commercially in the second half of 2009.

AzaSite Plus: Phase 3 Clinical Trials for Blepharitis/Blepharoconjunctivitis

Expansion of our AzaSite product into a larger franchise includes a fixed combination of azithromycin with dexamethasone for the treatment of blepharitis/blepharoconjunctivitis, an infection of the eyelid and the conjunctiva and one of the most common eye problems in older adults, as well as other ophthalmic infections. In 2006, we completed our preclinical development of this combination product candidate, filed an Investigational New Drug Application (IND) with the FDA and conducted a Phase 1 clinical trial.

In February 2007, we announced that the preliminary safety data from our Phase 1 trial indicated that AzaSite Plus was well tolerated and no serious adverse events were reported. Treatment-related ocular adverse events were minimal in frequency and equivalent between the treatment and placebo groups. There were no significant differences in intraocular pressure between the AzaSite Plus group and placebo group after 14 days of treatment.

In the fall of 2007, we conducted a pilot study to evaluate endpoints and time points for use in the Phase 3 trial for AzaSite Plus. There were 32 patients with blepharoconjunctivitis who completed the double-masked and randomized trial and received eye drops two times a day for 14 days. The results led to the selection of endpoints for the first Phase 3 trial, which included lid margin redness, lid swelling, conjunctival redness, ocular discharge and lid irritation in at least one eye.

The Phase 3 trial tested a total of 417 patients. The dosing regimen consists of one drop in the eye and one on the eyelid, two times a day for 14 days. The trial design included three treatment arms with the objective of demonstrating the superiority of AzaSite Plus in treating blepharoconjunctivitis over AzaSite alone or dexamethasone alone.

Results from the Phase 3 trial indicated that AzaSite Plus improved clinical outcomes as compared to treatment with AzaSite alone or dexamethasone alone in bacterial eradication and the reduction of inflammatory signs and symptoms, respectively. AzaSite Plus was very well tolerated. However, an evaluation of the data indicated that the trial did not achieve its primary endpoint as defined by the protocol.

In April 2009, we discussed the results of this trial with the FDA and, based on this meeting, we developed a pilot study protocol for the treatment of blepharitis that would seek to demonstrate AzaSite Plus's ability to delay exacerbation and/or recurrence of acute episodes of blepharitis. This study would serve as a basis for revisions to the pivotal Phase 3 clinical trial protocols.

In 2010, we discussed a development pathway for this product candidate with the FDA and are pursuing an SPA for the next Phase 3 clinical trial.

DexaSite: Met with the FDA to discuss the development pathway

We developed a topical formulation of the corticosteroid dexamethasone to treat eye inflammation caused by infections, injury, surgery or other conditions. In 2007, we completed our preclinical development of this product candidate. This is a second product candidate originating from the IND filed for AzaSite Plus.

In 2008, we determined that the data from our clinical trial indicated that DexaSite was well tolerated and no serious adverse events were reported with good efficacy. Treatment-related ocular adverse events were minimal in frequency and equivalent between all groups. There were no significant differences in intraocular pressure between the DexaSite group and the other group containing dexamethasone after 14 days of treatment.

In 2010, we discussed a development pathway for this product candidate with the FDA and are pursuing an SPA for the next Phase 3 clinical trial.

ISV-303: Phase 1/2 clinical trial for post-operative inflammation and eye pain

We developed a topical formulation of the non-steriodal anti-inflammatory bromfenac to treat post-operative inflammation and eye pain in patients who have undergone cataract extraction. In the first half of 2010, we completed our preclinical development of this product candidate and filed an IND with the FDA. In the second half of 2010, we initiated and completed enrollment for the Phase 1/2 clinical trial for this product candidate. In the first half of 2011, we expect to complete the clinical trials and have top-line results from this study.

ISV-101: Filed an IND for this product candidate

We developed a topical formulation of the non-steriodal anti-inflammatory bromfenac to treat dry eye disease. In January 2011, we filed an IND with the FDA. We anticipate a Phase 1/2 clinical trial for this product candidate.

DuraSite Sustained Delivery Technology

At the core of our AzaSite franchise is our proprietary DuraSite drug delivery technology. Our DuraSite sustained drug delivery technology is a synthetic polymer-based formulation designed to extend the residence time of a drug relative to conventional topical therapies. It enables topical delivery of a drug as a solution, gel, or suspension and can be customized for delivering a wide variety of potential drug candidates.

The combination of DuraSite and proven drug products results in differentiated products that have increased efficacy and improved compliance through a reduced dosing frequency that yields better outcomes; lowers the development risk by using the proven DuraSite technology with a proven drug product; and lowers development

costs. In addition to its formulation with azithromycin in our AzaSite family of products, our DuraSite technology may be used in the formulation of new ocular product candidates using either non-proprietary drugs or compounds developed by others for non-ophthalmic indications.

Physical Properties. DuraSite is composed of a cross-linked polyacrylic acid polymer, water and salts. We have developed considerable knowledge of how to formulate it for topical applications that have a range of viscosities and physical forms including gels, suspensions and solutions. The size of the dry polymer particle averages 5 microns. The molecular weight of the polymer exceeds $3x10^7$ Daltons. Upon the addition of water, DuraSite swells to ~100x its original weight.

The polymer entraps water and the active drug product in a bioadhesive matrix. The viscosity of the matrix is controlled by pH. The bioavailability and release characteristics of the drug can be adjusted by altering the chemical environment. The resulting drug delivery system is bioadhesive, sustained release, and compatible with both water soluble and water insoluble molecules.

Regulatory Status. The ingredients in the DuraSite sustained release technology are classified by the FDA as Category 1 GRAS (generally regarded as safe). It has been approved by many pharmacopeias, which helps to facilitate worldwide approvals of drugs that contain it. DuraSite has been used commercially in AquaSite, an ophthalmic product for dry eye syndrome, and in AzaSite, a topical anti-infective product for the treatment of bacterial conjunctivitis. It is also utilized in Bausch & Lomb's new anti-infective eye drop Besivance, besifloxacin ophthalmic suspension, 0.6%, which was approved by the FDA in May 2009. Bausch & Lomb launched this product in the second half of 2009.

Additional Research and Development Opportunities

In addition to products leveraging our DuraSite technology, we will seek to in-license or acquire promising product candidates and technologies from academic institutions and other companies and to apply our expertise to create novel differentiated ophthalmic product opportunities.

Collaborative, Licensing and Service Agreements

As part of our business strategy, we have entered into, and will continue to pursue additional licensing agreements, corporate collaborations and service contracts. In our international licensing agreements, the licensee is responsible for obtaining regulatory approval and will generally pay us a double digit royalty on net sales of AzaSite in these countries, if approved by regulatory authorities. We will be responsible for providing AzaSite inventory to these licensees at a fee set forth in each respective license agreement. There can be no assurance that we will be able to negotiate acceptable collaborative, licensing or service agreements, or that our existing arrangements will be successful or renewed or that it will not be terminated.

Pfizer Inc. and Pfizer Products, Inc. In February 2007, we entered into a worldwide, exclusive, royalty-bearing licensing agreement with Pfizer, under Pfizer's patent family titled "Method of Treating Eye Infections with Azithromycin" for ocular anti-infective product candidates known as AzaSite and AzaSite Plus. Under the Pfizer License, we are required to pay Pfizer a single-digit royalty based on net sales of the licensed products and to use reasonable commercial efforts to seek regulatory approval for and market licensed products. We have the right to grant sublicenses, subject to Pfizer's prior approval which shall not be unreasonably withheld.

Inspire Pharmaceuticals, Inc. In February 2007, we entered into a license agreement, or the Inspire License, with Inspire under which we licensed exclusive development and commercialization rights, under our AzaSite patent rights and certain know-how, for topical anti-infective products containing azithromycin as the sole active ingredient for human ocular or ophthalmic indications in the United States and Canada and their respective territories. The Inspire License also provides for nonexclusive licenses under our DuraSite patent rights, container patent rights, Columbia Laboratories, Inc. polymer technology patent rights and certain know-how in

the same field of use as described above. We also granted Inspire an exclusive sublicense under the Pfizer patent rights that we have licensed under the Pfizer License discussed above. Inspire has the right to grant sublicenses under the terms of the Inspire License.

Upon the closing of the Inspire License, Inspire paid us license fees and a milestone payment totaling $32 million through FDA approval in April 2007. Inspire also pays us a royalty on net sales. The royalty rate was 20% on net sales in the first two years of commercialization and is now 25%. Inspire is obligated to pay us royalties under the Inspire License for the longer of (i) eleven years from the launch of the first product (August 13, 2007) and (ii) the period during which a valid claim under a patent licensed from us covers a licensed product. For five years after the first year of commercial sale, Inspire is required to pay us the greater of the royalty discussed above or certain tiered minimum royalties. The royalties discussed above are subject to certain reductions in the event of patent invalidity, third party licenses, generic competition and uncured material breach.

Under the Inspire License, we were responsible for obtaining regulatory approval of AzaSite in the U.S. which occurred in April 2007. We subsequently transferred regulatory documentation regarding AzaSite, including the New Drug Application (NDA), to Inspire. We were also responsible for obtaining regulatory approval of AzaSite in Canada. In March 2009, the Therapeutic Products Directorate of Health Canada approved the new drug submission (NDS) for AzaSite in Canada. Within 25 days after obtaining regulatory approval for Canada, we transferred regulatory documentation regarding AzaSite to Inspire. Thereafter, Inspire is responsible for all regulatory obligations and strategies relating to the further development and commercialization of products in each country. Inspire will also be responsible for commercialization in both the U.S. and Canada. In the United States, Inspire focuses on ophthalmologists and optometrists who routinely treat eye infections.

We are obligated to provide to Inspire certain future developments, including know-how and patent rights, developed up to the effective transfer date of the regulatory documentation in the U.S. and Canada that are necessary or useful to develop or commercialize any product for bacterial conjunctivitis in those countries. Such developments will be provided without additional fees but any product that includes such developments will be subject to the same royalty rates described above. For certain further developments after such regulatory transfer date, Inspire has a time-limited exclusive option to license such further developments upon terms and conditions to be separately negotiated.

In addition, we also entered into a trademark license agreement with Inspire in February 2007 under which we granted to Inspire an exclusive license to the AzaSite trademark and domain name and a nonexclusive license to the DuraSite trademark in connection with the commercialization of products in the U.S. and Canada under the terms of the Inspire License.

We also entered into a supply agreement, or the Supply Agreement, with Inspire in February 2007 for azithromycin. We had previously entered into a third-party supply agreement for the production of azithromycin. Under the Supply Agreement, we agreed to supply Inspire's requirements of azithromycin, pursuant to certain forecasting and ordering procedures. The initial term of the Supply Agreement expires in 2012, subject to customary termination provisions, such as termination for material breach. Either party may terminate the Supply Agreement upon 180 days notice to the other party. In addition, Inspire may terminate the Supply Agreement if our third party supplier moves the location at which the active ingredient is manufactured. After 2012, the Supply Agreement automatically renews for successive three-year periods unless terminated pursuant to the foregoing termination provisions. If we are in breach of our supply obligations under the Supply Agreement, Inspire is permitted to qualify a second source supplier, at our expense, and obtain the active ingredient from such second source. We are obligated under the Supply Agreement to maintain a minimum quantity of the active ingredient in inventory for Inspire's use in manufacturing the licensed products and to maintain the quality agreement negotiated with the supplier. The Supply Agreement also contains certain provisions regarding the rights and responsibilities of the parties with respect to manufacturing specifications, delivery arrangements, quality assurance, regulatory compliance, product recall and indemnification, as well as certain other customary matters.

During the years ended December 31, 2010, 2009 and 2008, our licensee, Inspire, represented approximately 92%, 85% and 100%, respectively, of our total revenues.

Catalent Pharma Solutions, formerly Cardinal Health PTS, L.L.C. In September 2005, we entered into a commercial manufacturing supply agreement with Catalent Pharma Solutions, or Catalent for the manufacture of AzaSite commercial units. The agreement had a term of four years subsequent to the approval by the FDA of Catalent as a manufacturer of AzaSite. Payments under the contract are dependent upon rolling production forecasts we provide to Catalent and are subject to certain minimum purchase commitments which escalate over the term of the contract. According to plan, the AzaSite NDA was transferred to Inspire and manufacturing responsibilities for AzaSite were transferred to Inspire for manufacturing AzaSite for the U.S. and Canada. We continue to have a relationship with Catalent for the manufacture of AzaSite for international partners as well as for other products in our pipeline.

Bausch and Lomb Incorporated. In December 2003, we completed the sale of our drug candidate for the treatment of ocular infections to Bausch & Lomb Incorporated or Bausch & Lomb, pursuant to a Purchase Agreement and a License Agreement, or the License Agreement, and collectively, the Asset Sale. The drug candidate, Besivance, was developed by Bausch & Lomb. In May 2009, the FDA approved Besivance to treat bacterial conjunctivitis (pink eye). Besivance was launched in the United States by Bausch & Lomb and Pfizer, Inc. in the second half of 2009.

We are entitled to a single-digit royalty on future Besivance net product sales, if any, in all licensed countries, ending upon the later of the expiration of the patent rights underlying Besivance or ten years from the date of the first Besivance product sale by Bausch & Lomb. Bausch & Lomb has assumed all future Besivance development and commercialization expenses and is responsible for all development activities.

The License Agreement provides Bausch & Lomb a license under certain of our patents related to our DuraSite delivery system for use with Besivance and under other non-patented intellectual property used in Besivance. The License Agreement provides for Bausch & Lomb to complete development of the SS734 fluoroquinolone products that combine certain compounds we licensed from SSP Co., Ltd. (SSP) with the DuraSite delivery system and to commercialize any such products. The patent license is exclusive in the particular field of developing, testing, manufacturing, obtaining regulatory approval of, marketing, selling and otherwise disposing of such products. The license of non-patented intellectual property granted to Bausch & Lomb is nonexclusive.

In connection with the Asset Sale, we also assigned to Bausch & Lomb an agreement between SSP and us under which we were licensed to commercialize SSP's SS734 fluoroquinolone. Because that agreement also included a license from us to SSP of certain patents relating to DuraSite that we did not sell to Bausch & Lomb, the assignment of the agreement to Bausch & Lomb excluded the assignment of our obligations and rights as the licensor of such patents. Instead, we entered into a new license agreement with SSP reflecting our original rights and obligations as the licensor of the DuraSite patents to SSP.

Other. As part of our basic strategy, we continually pursue agreements with other companies, universities and research institutions concerning additional therapeutic agents and drug delivery technologies to complement and expand our family of proprietary ophthalmic products as well as collaborative agreements for the further development and marketing of our current products and product candidates. We intend to continue exploring licensing and collaborative opportunities, although there is no certainty that we can successfully enter into, or maintain, any such agreements.

Patents and Proprietary Rights

Patents and other proprietary rights are important to our business. Our policy is to file patent applications seeking to protect technology, inventions and improvements to our inventions that we consider valuable. We also

rely upon trade secrets, know-how, continuing technological innovations and licensing opportunities to develop and maintain our competitive position. Our DuraSite drug delivery products are made under patents and applications, and we have filed a number of patent applications in the United States relating to our DuraSite technology with delivery tips and drug compounds. Of these applications, eight U.S. patents have been issued. We have four U.S. patents on our retinal drug delivery device that have been issued. Six U.S. patents have been issued related to our antibiotic programs with two applications pending. At least six other patent applications by us relating to the foregoing and other aspects of our business and potential business are also pending. Foreign counterparts of our patents as well have filed/issued in many countries.

The patent positions of pharmaceutical companies, including ours, are uncertain and involve complex legal and factual questions. In addition, the coverage claimed in a patent application can be significantly reduced before a patent is issued. Consequently, we do not know whether any of our pending patent applications will result in the issuance of patents or if any of our patents will provide significant proprietary protection. Since patent applications are maintained in secrecy until they are published, we cannot be certain that we or any licensor was the first to file patent applications for such inventions or that patents issued to our competitors will not block or limit our ability to exploit our technology. Moreover, we might have to participate in interference proceedings declared by the U.S. Patent and Trademark Office, or USPTO, to determine priority of invention, which could result in substantial cost to us, even if the eventual outcome were favorable. There can be no assurance that our patents will be held valid or enforceable by a court or that a competitor's technology or product would be found to infringe such patents. See Item 3. "Legal Proceedings."

A number of pharmaceutical companies and research and academic institutions have developed technologies, filed patent applications or received patents on various technologies that may be related to our business. Some of these technologies, applications or patents may conflict with our technologies or patent applications. This conflict could limit the scope of the patents, if any, that we may be able to obtain or result in the denial of our patent applications. In addition, if patents that cover our activities have been or are issued to other companies, there can be no assurance that we would be able to obtain licenses to these patents at a reasonable cost or at all, or be able to develop or obtain alternative technology. If we do not obtain such licenses, we could encounter delays in or be precluded altogether from introducing products to the market.

In addition to patent protection, we also rely upon trade secret protection for our confidential and proprietary information. There can be no assurance that others will not independently develop substantially equivalent proprietary information and techniques or otherwise gain access to our trade secrets, that such trade secrets will not be disclosed or that we can effectively protect our rights to unpatented trade secrets.

We believe our drug delivery technology may expand the ophthalmic pharmaceutical market by permitting the novel use of drugs for ophthalmic indications that are currently used or being developed for non-ophthalmic indications. However, we may be required to obtain licenses from third parties that have rights to these compounds in order to conduct research, to develop or to market products that contain such compounds. There can be no assurance that such licenses will be available on commercially reasonable terms, if at all.

Research and Development

On December 31, 2010, our research and development staff numbered 5 people, of whom 2 have Ph.D.s. Our research and development expenses for the years ended December 31, 2010, 2009 and 2008 were, as follows:

Research and Development Cost by Program
(in millions)

Program	2010	2009	2008
ISV-303	$ 1.3	$ 0.2	$ —
AzaSite Plus	0.1	0.2	7.6
AzaSite	0.1	0.1	0.2
ISV-016	—	—	0.4
New products and other	0.6	0.1	0.9
Programs - non-specific	2.9	4.8	7.1
Total	$ 5.0	$ 5.4	$16.2

In 2010, program expenses primarily consisted of non-specific program costs which comprised facility, internal personnel and stock-based compensation costs that are not allocated to a specific development program. The non-specific costs decrease in 2010, as compared to 2009, was primarily due to savings resulting from the Company's corporate restructuring in March 2009. Our ISV-303 program expenses primarily related to preclinical experiments and the Phase 1/2 clinical trial that was initiated in August 2010. Other program activities consisted primarily of new product development.

In 2009, program expenses primarily consisted of non-specific program costs which comprised facility, internal personnel, and stock-based compensation costs that are not allocated to a specific development program. The non-specific costs decreased from 2008 due to our corporate restructuring. Our AzaSite Plus program expenses consisted of ongoing consulting and data analysis pertaining to our Phase 3 clinical trial. Other program activities consisted primarily of activities related to commercializing AzaSite in international markets.

In 2008, program expenses primarily consisted of non-specific program costs, our AzaSite Plus Phase 3 clinical trial and preparation for the production of Canadian AzaSite registration batches at our contract manufacturing site. Our activities related to ISV-016 mainly consisted of preclinical testing prior to its discontinuation in July 2008. Other program activities consisted primarily of new product development and activities related to commercializing AzaSite in the international markets.

Manufacturing

We have no experience or facilities for the manufacture of products for commercial purposes and we currently have no intention of developing such experience or building such facilities. We have a pilot facility, licensed by the State of California, to produce potential products for Phase 1 and some of our Phase 2 clinical trials. However, we rely on third parties for supplies and materials necessary for our Phase 3 clinical trials and commercial needs. If we should encounter delays or difficulties in establishing and maintaining our relationship with qualified manufacturers to produce, package and distribute our finished products, then clinical trials, regulatory filings, market introduction and subsequent sales of such products would be adversely affected.

We have entered into a licensing agreement with Inspire under which they are responsible for the manufacture of AzaSite for the United States and Canada. The AzaSite NDA was transferred to Inspire and manufacturing responsibilities for AzaSite were transferred to Inspire for the U.S. and Canada. We have a relationship with Catalent for the manufacture of AzaSite for international partners as well as for other products in our pipeline.

Marketing and Sales

The cost to develop and maintain a marketing organization and sales force is significant and would result in the reallocation of resources needed for the development of our product candidates. We do not currently plan on establishing a dedicated sales force or a marketing organization for our AzaSite, AzaSite Plus or other product candidates.

We have entered into corporate collaborations, and we may continue to pursue additional collaborations with one or more additional pharmaceutical companies in the U.S. and abroad, to market our products. In international licensing agreements, the licensee is responsible for obtaining regulatory approval and will generally pay the Company a double-digit royalty on net sales of AzaSite in these countries, if approved by regulatory authorities. We will be responsible for providing AzaSite inventory to these licensees at a fee per respective agreed upon licensing agreement. There can be no assurance that we will be able to negotiate acceptable collaborative, licensing or service agreements, or that our existing arrangements will be successful or renewed or that it will not be terminated.

Inspire Pharmaceuticals, Inc. In February 2007, we entered into an exclusive agreement with Inspire under which Inspire obtained the right to exclusively market AzaSite in the United States and Canada. We received a licensing fee, a milestone payment when AzaSite was approved by the FDA and received the first royalty payment based on net sales of the product in the third quarter 2007.

Bausch & Lomb. In December 2003, we sold our product candidate to Bausch & Lomb. Bausch & Lomb has the exclusive marketing rights for the world except for Japan, which were retained by SSP, and shared rights in the rest of Asia with SSP. Bausch & Lomb has also assumed the development and manufacturing responsibilities for the product formulation for their sales and distribution and we are entitled to royalties based on net sales of the product, if any. The drug candidate, Besivance, was developed by Bausch & Lomb and approved by the FDA in May 2009. Besivance was launched in the United States by Bausch & Lomb and Pfizer, Inc. in the last half of 2009.

Competition

The pharmaceutical industry is highly competitive and requires an ongoing commitment to the pursuit of technological innovation. Such commitment requires significant investment in the resources necessary to discover, develop, test and obtain regulatory approvals for products. It also involves the need to effectively commercialize, market and promote approved products, including communicating the effectiveness, safety and value of products to customers and medical professionals.

The global ophthalmic market is anticipated to grow and will become even more competitive going forward as the prevalence of eye disease increases, leading to increased demand for new and novel ophthalmic products. The market segments that treat diseases and conditions of the eye are subject to ongoing technological change and evolution.

Many companies are engaged in activities similar to our own. Some of these companies have substantially greater financial, technical, marketing and human resources available to them, which may allow them to succeed in developing technologies and products at a faster rate, thereby gaining greater market acceptance than the therapies that we are developing or have developed with our more limited resources. By being first to the market, these competitors may also succeed in obtaining cost advantages or intellectual property rights that would limit our ability to develop and commercialize our own product opportunities. Consequently, they might obtain a more timely and effective regulatory approval for the commercialization of their products in comparison to our timeline.

The global ophthalmic pharmaceutical market is currently dominated by a number of large and well-established companies, including Alcon Laboratories, Inc., Allergan, Inc., Bausch & Lomb, Novartis

Ophthalmics, Johnson & Johnson, Merck & Co., and Pfizer. While there are many other large- and medium-sized companies participating in the ophthalmic market, smaller companies such as our own find it challenging to successfully develop and market products without entering into collaborations.

Certain segments of the greater ophthalmic market, such as those for glaucoma, anti-infective, and anti-inflammatory agents, already have well-established competing products currently available as well as many in development by prominent competitors. Therefore, in order to penetrate these competitive mature markets, new products must exhibit improved efficacy and safety profiles, be supported by strong marketing and sales initiatives, and have the support of industry thought leaders.

In summary, our competitive position will depend on our ability to develop enhanced and innovative products, maintain a proprietary position in our technology, obtain required government approvals for our products on a timely basis, attract and retain key personnel, and enter into effective collaborations for the manufacture, commercial marketing and distribution of our products in key worldwide markets.

Government Regulation

The manufacturing and marketing of our products and our research and development activities are subject to regulation by numerous governmental authorities in the United States and other countries. In the United States, drugs are subject to rigorous FDA regulation. The Federal Food, Drug and Cosmetic Act and regulations promulgated there under govern the testing, manufacture, labeling, storage, record keeping, approval, advertising and promotion in the United States of our products. In addition to FDA regulations, we are also subject to other federal and state regulations such as the Occupational Safety and Health Act and the Environmental Protection Act. Product development and approval within this regulatory framework takes a number of years and involves the expenditure of substantial resources.

The steps required before a pharmaceutical agent may be marketed in the United States include:

- preclinical laboratory;
- submission to the FDA of an IND;
- adequate and well-controlled human clinical trials to establish the safety and efficacy of the drug;
- the submission of an NDA or Biological License Application (“BLA”) to the FDA; and
- the FDA approval of the NDA or BLA, prior to any commercial sale or shipment of the drug.

In addition to obtaining FDA approval for each product, each domestic drug manufacturer and facility must be registered with, and approved by, the FDA. Drug product manufacturing establishments located in California also must be licensed by the State of California in compliance with separate regulatory requirements.

Preclinical tests include laboratory evaluation of product chemistry and animal studies to assess the potential safety and efficacy of the product and its formulation. The results of the preclinical tests are submitted to the FDA as part of an IND and, unless the FDA objects, the IND will become effective 30 days following its receipt by the FDA.

Clinical trials involve the administration of the drug to healthy volunteers or to patients under the supervision of a qualified principal investigator. Clinical trials are conducted in accordance with protocols that detail the objectives of the study, the parameters to be used to monitor safety and the efficacy criteria to be evaluated. Before any clinical trial can commence, each protocol is submitted to the FDA as part of the IND. Each clinical study is conducted under the auspices of an independent Institutional Review Board that considers, among other things, ethical factors and the rights, welfare and safety of human subjects.

Clinical trials are typically conducted in three sequential phases, but the phases may involve multiple studies and may overlap. In Phase 1, the initial introduction of the drug into human subjects, the drug is tested for safety

(adverse effects), dosage tolerance, metabolism, distribution, excretion and clinical pharmacology. Phase 2 involves studies in a limited patient population to (i) determine the efficacy of the drug for specific targeted indications, (ii) determine dosage tolerance and optimal dosage and (iii) identify possible adverse effects and safety risks. When a compound is found to be effective and to have an acceptable safety profile in Phase 2 evaluations, Phase 3 trials are undertaken to further evaluate clinical efficacy and to further test for safety within an expanded patient population at multiple clinical study sites. The FDA reviews both the clinical plans and the results of the trials and may discontinue the trials at any time if there are significant safety issues.

The results of the preclinical studies and clinical studies are submitted to the FDA in the form of an NDA or BLA for marketing approval. The testing and approval process requires substantial time and effort and there can be no assurance that any approval will be granted on a timely basis, if at all. Additional animal studies or clinical trials may be requested during the FDA review period and may delay marketing approval. After FDA approval for the initial indications, further clinical trials are necessary to gain approval for the use of the product for additional indications. The FDA may also require post-marketing testing to monitor for adverse effects, which can involve significant expense.

Among the conditions for manufacture of clinical drug supplies and for NDA or BLA approval is the requirement that the prospective manufacturer's quality control and manufacturing procedures conform to current Good Manufacturing Practice, or cGMP. Prior to approval, manufacturing facilities are subject to FDA and/or other regulatory agency inspection to ensure compliance with cGMP. Manufacturing facilities are subject to periodic regulatory inspection to ensure ongoing compliance.

For marketing outside the United States, we or our licensees are also subject to foreign regulatory requirements governing human clinical trials and marketing approval for drugs. The requirements governing the conduct of clinical trials, product licensing, pricing and reimbursement vary widely from country to country and in some cases are even more rigorous than in the United States.

Scientific and Business Advisors

We have access to a number of academic and industry advisors with expertise in clinical ophthalmology and pharmaceutical development, marketing and sales. Our advisors meet with our management and key scientific employees on an ad hoc basis to provide advice in their respective areas of expertise and further assist us by periodically reviewing with management our preclinical, clinical and marketing activities. We plan to make arrangements with other individuals to join as advisors as appropriate. Although we expect to receive guidance from our advisors, all of our advisors are employed on a full-time basis by other entities, or are primarily engaged in outside business activities, and may have other commitments to, or consulting or advisory contracts with, other entities that may conflict or compete with their obligations to us.

Executive Officers and Other Officers of the Company

As of March 4, 2011, our executive officers and other officers were as follows:

Name	Age	Title
Timothy Ruane	46	Chief Executive Officer and member of the Board
Louis Drapeau	67	Vice President and Chief Financial Officer
Lyle M. Bowman, Ph.D.	62	Vice President, Development
Kamran Hosseini, M.D., Ph.D.	46	Vice President, Clinical Affairs and Chief Medical Officer
Surendra Patel	56	Vice President, Operations

Timothy Ruane joined us on December 1, 2010 as Chief Executive Officer and was elected as a member of the Board. Previously, Mr. Ruane served as President and Chief Executive Officer of Tekmira Pharmaceuticals

and INEX Pharmaceuticals (which spun-out to Tekmira in 2007), a biopharmaceutical company, from 2005 to 2008. From 2004 to 2005, he served as the Senior Vice President of Corporate Development of INEX. From 2002 to 2004, Mr. Ruane was the Senior Vice President of Business Management of ILEX Oncology. Mr. Ruane has more than 24 years of experience with pharmaceutical and biotechnology companies in various management positions. Mr. Ruane has a Bachelor of Science degree in business finance from Wake Forest University and a masters in business administration from the University of Washington.

Louis Drapeau joined us on October 1, 2007 as Vice President and Chief Financial Officer and served as the interim Chief Executive Officer from October 2008 to November 2010. Mr. Drapeau served as Senior Vice President, Finance and Chief Financial Officer of Nektar Therapeutics, a biopharmaceutical company, from January 2006 until September 2007. From August 2002 to August 2005, Mr. Drapeau was Senior Vice President and Chief Financial Officer of BioMarin Pharmaceutical, a fully integrated biopharmaceutical company. From August 2004 to May 2005, Mr. Drapeau also held the position of Acting Chief Executive Officer of BioMarin. Prior to that, Mr. Drapeau spent over 30 years with Arthur Andersen including 19 years as an Audit Partner in Arthur Andersen's Northern California Audit and Business Consulting practice which also included 12 years as Managing Partner. He holds an undergraduate degree in mechanical engineering and masters in business administration from Stanford University.

Lyle M. Bowman joined us in October 1988 as Director of Drug Delivery Systems. Previously, Dr. Bowman had worked at Syntex Ophthalmics as Manager/Director of Analytical Polymer Characterization working on contact lenses and solutions from 1979 through September 1988. From 1989 to 1991, Dr. Bowman served as Vice President, Science and Technology. From 1991 to 1995, he served as Vice President, Development, and from 1995 to 2008 served as Vice President Development and Operations. Dr. Bowman currently is Vice President Development, holds a Ph.D. in Physical Chemistry from the University of Utah and has considerable experience in material science as applied to ophthalmic products.

Kamran Hosseini joined us in February 2008 as Vice President, Clinical Affairs and Chief Medical Officer. From November 2007 to February 2008, Dr. Hosseini served as the ophthalmic expert at JGB BioPharma consulting for R&D, preclinical, clinical, and business development projects. From May 2005 to October 2007, he was the director of ophthalmology drug delivery programs at Alza Corporation, a member of the Johnson and Johnson Family of Companies, where he provided ophthalmology and visual science expertise for new technology assessment activities aimed at enhancing the drug/device unit pipeline. From November 2003 to May 2005, he was a post doctoral fellow in retinal degenerative diseases at the University of California, San Francisco. Dr. Hosseini received his M.D. from the University of Groningen Faculty of Medicine, The Netherlands; and his Ph.D. as part of a joint program at the University of Texas, Medical Branch in Galveston and the University of Maastricht, The Netherlands.

Surendra Patel joined us in April 2008 as Vice President, Operations. From 2002 to 2008, Mr. Patel served as Senior Director, Manufacturing Operations at Nektar Therapeutics where he managed clinical and commercial manufacturing operations and played a strategic role in the selection of domestic and international contract manufacturing sites. Mr. Patel has more than 30 years of development and operational experience in various management positions at pharmaceutical and biotechnology companies, including Syntex, Roche Bioscience, Oread Inc., and DrugAbuse Sciences. Mr. Patel has a Bachelor of Science degree in pharmaceutical formulation from De Montford University, Leicester, United Kingdom.

Officers are appointed to serve at the discretion of the Board of Directors until their successors are appointed. There are no family relationships between any members of our Board of Directors and our executive officers.

Employees

As of December 31, 2010, we had 12 employees, 10 of whom were full time. None of our employees are covered by a collective bargaining agreement. We believe we have good employee relations. We also utilize independent consultants to provide services in certain areas of our scientific and business operations.

Item 1A. Risk Factors

Risks Relating to Our Business

It is difficult to evaluate our business because we are in an early stage of commercializing our products, our technology is untested and successful development of pharmaceutical products is highly uncertain and requires significant expenditures and time

We are in the early stages of commercializing our products. AzaSite received regulatory approval in April 2007 and commercial sales of AzaSite began in the third quarter of 2007. Besivance received regulatory approval in May 2009 and commercial sales of Besivance began in the second half of 2009. We must receive approval in other countries prior to marketing AzaSite in such countries. Before regulatory authorities grant us marketing approval for additional products, we need to conduct significant additional research and development and preclinical and clinical testing and submit a New Drug Application ("NDA"). Successful development of pharmaceutical products is highly uncertain. Products that appear promising in research or development, may be delayed or fail to reach later stages of development or the market for several reasons, including:

- preclinical tests may show the product to be toxic or lack efficacy in animal models;
- failure to receive the necessary United States and international regulatory approvals or a delay in receiving such approvals. Among other things, such delays may be caused by slow enrollment in clinical studies; failure to achieve study endpoints within the time period prescribed by the study, or at all; additional time requirements for data analysis or Biologic License Application or NDA preparation; discussions with the FDA; FDA requests for additional preclinical or clinical data; analyses or changes to study design; or unexpected safety, efficacy or manufacturing issues;
- enrollment in clinical studies; failure to achieve study endpoints within the time period prescribed by the study, or at all; additional time requirements for data analysis or Biologic License Application or NDA preparation; discussions with the FDA; FDA requests for additional preclinical or clinical data; analyses or changes to study design; or unexpected safety, efficacy or manufacturing issues;
- clinical trial results may show the product to be less effective than desired or to have harmful or problematic side effects;
- difficulties in formulating the product, scaling the manufacturing process, or getting approval for manufacturing;
- even if safe and effective, manufacturing costs, pricing, reimbursement issues, or other factors may make the product uneconomical;
- proprietary rights of others and their competing products and technologies may prevent the product from being developed or commercialized; or
- inability to compete with superior, equivalent, more cost-effective or more effectively promoted products offered by competitors.

Therefore, our research and development activities may not result in any commercially viable products.

We have a history of operating losses and we expect to continue to have losses in the future

We have incurred significant operating losses since our inception in 1986 and have pursued numerous drug development candidates that did not prove to have commercial potential. We expect to incur net losses for the foreseeable future or until we are able to achieve significant royalties or other revenues from sales of our products. Attaining significant revenue or profitability depends upon our ability, alone or with third parties, to develop our potential products successfully, conduct clinical trials, obtain required regulatory approvals and manufacture and market our products successfully. We may not ever achieve or be able to maintain significant revenue or profitability, including with respect to AzaSite, our lead product which has not yet been commercially launched outside the United States.

Clinical trials, such as the recently announced ISV-303 clinical trial, are expensive, time-consuming and difficult to design and implement and there can never be any assurance that the results of such clinical trials will be favorable

Human clinical trials for our product candidates are very expensive and difficult to design and implement, in part because they are subject to rigorous regulatory requirements. The clinical trial process is also time-consuming. We estimate that any particular clinical trial may take over a year to complete. Furthermore, we could encounter problems that might cause us to abandon or repeat clinical trials resulting in additional expense, further delays and potentially preventing the completion of such trials. The commencement and completion of clinical trials may be delayed or terminated due to several factors, including:

- unforeseen safety issues;
- lack of effectiveness during clinical trials;
- difficulty in determining dosing and trial protocols;
- slower than expected rates of patient recruitment;
- inability to monitor patients adequately during or after treatment; and
- inability or unwillingness of clinical investigators to follow our clinical protocols.

In addition, we or the FDA may suspend our clinical trials at any time if it appears that we are exposing participants to unacceptable health risks or if the FDA finds deficiencies in our submissions or the conduct of these trials. In any such case, including with respect to the ISV-303 clinical trial, we may not be able to obtain regulatory approval for our product candidates, in which case we would not obtain any benefit from our substantial investment in developing the product and conducting clinical trials for such products.

The results of our clinical trials may not support our product candidate claims

Even if our clinical trials, such as the recently announced ISV-303 clinical trial, are completed as planned, we cannot be certain that the results will support our product candidate claims. Even if pre-clinical testing and early clinical trials for a product candidate are successful, this does not ensure that later clinical trials will be successful and we cannot be sure that the results of later clinical trials will replicate the results of prior clinical trials and pre-clinical testing or meet our expectations. The clinical trial process may fail to demonstrate that our product candidates are safe for humans or effective for indicated uses. In addition, our clinical trials involve relatively small patient populations. Because of the small sample size, the results of these clinical trials may not be indicative of future results. Any such failure would likely cause us to abandon the product candidate and may delay development of other product candidates. Any delay in, or termination of, our clinical trials will delay or preclude the filing of our NDAs with the FDA and, ultimately, our ability to commercialize our product candidates and generate product revenues.

For example, results from our Phase 3 clinical trial of AzaSite Plus for the treatment of blepharoconjunctivitis showed improved clinical outcomes as compared to treatment with a corticosteroid alone or antibiotic alone in the reduction of inflammatory signs and symptoms and bacterial eradication, respectively. In addition, AzaSite Plus was very well tolerated. However, the trial did not achieve its primary endpoint as defined by the protocol. We discussed the results of this trial with the FDA and determined a development plan for AzaSite Plus. The initiation of any further clinical studies of AzaSite Plus is currently on hold pending the outcome of our evaluation of our strategic opportunities. We cannot assure you that any additional clinical trials for AzaSite Plus will be conducted or, if conducted, that they will meet the prescribed clinical endpoint as defined in the protocol for that study or that we will ultimately achieve FDA approval for the commercialization of AzaSite Plus.

Our strategy for commercialization of our products requires us to enter into successful arrangements with corporate collaborators

We generally intend to enter into partnering and collaborative arrangements with respect to the commercialization of our product candidates, such as AzaSite Plus and ISV-303. However, we cannot assure you that we will be able to enter into such arrangements or that they will be beneficial to us. The success of our partnering and collaboration arrangements will depend upon many factors, including:

- the progress and results of our preclinical and clinical testing and research and development programs;
- the time and cost involved in obtaining regulatory approvals;
- our ability to negotiate favorable terms with potential collaborators;
- the efforts and success of our collaborators in further developing or marketing the product;
- our ability to prosecute, defend and enforce patent claims and other intellectual property rights;
- the outcome of possible future legal actions; and
- competing technological and market developments.

We may not be able to conclude arrangements with third parties to support the commercialization of our products on acceptable terms, or at all, and may not be able to maintain any arrangement that we do enter into. If we pursue a partnership for AzaSite Plus or our other product candidates prior to completing the Phase 3 trials, we will likely receive less favorable economic terms than if we completed successful Phase 3 trials.

The commercial success of our products is dependent on the diligent efforts of our corporate collaborators

Because we generally rely on third parties for the marketing and sale of our products, revenues that we receive will be highly dependent on the efforts and success of these third parties, particularly our partner Inspire. These partners may terminate their relationships with us and/or may not diligently or successfully market or sell our products. These partners may also pursue alternative or competing technologies or develop alternative products either on their own or in collaboration with others, including our competitors. In addition, marketing consultants and contract sales organizations that we may use in the future for our products may market products that compete with our products and we must rely on their efforts and ability to market and sell our products effectively.

If we fail to enter into future collaborations or our current collaborations are terminated, we will need to enter into new collaborations or establish our own sales and marketing organization

We may not be able to enter into or maintain collaborative arrangements with third parties. If we are not successful in entering into future collaborations or maintaining our existing collaborations, particularly with Inspire, we may be required to find new corporate collaborators or establish our own sales and marketing organization. Under the terms of the Inspire License Agreement, Inspire may terminate the agreement at any time. If Inspire were to terminate the agreement, we would have to find a new marketing partner or market AzaSite ourselves. There can be no assurance that any new partnership would be on the similar terms as the Inspire License Agreement. We have no experience in sales, marketing or distribution and establishing such an organization would be costly. Moreover, there is no guarantee that a sales and marketing organization would be successful once established. If we are unable to maintain existing collaborations, enter into additional collaborations or successfully market our products ourselves, our revenues and financial results would be significantly harmed.

Our future success depends on our ability to engage third parties to assist us with the development of new products, new indications for existing products and in the conduct of our clinical trials to achieve regulatory approval for commercialization and any failure or delay by those parties to fulfill their obligations could adversely affect our development and commercialization plans

For our business model to succeed, we must continually develop new products or discover new indications for our existing products. As part of that process, we rely on third parties such as clinical research organizations,

clinical investigators and outside testing labs for development activities, such as Phase 2 and/or Phase 3 clinical testing, and to assist us in obtaining regulatory approvals for our product candidates. We rely heavily on these parties for successful execution of their responsibilities but have no control over how these parties manage their businesses and cannot assure you that such parties will diligently or effectively perform their activities. For example, the clinical investigators conducting our clinical trials, including our first Phase 3 trial for AzaSite Plus and Phase 1/2 trial for ISV-303, were not our employees and we anticipate that any future Phase 3 trials of AzaSite Plus or ISV-303 will also be conducted by a third party. However, we are responsible for ensuring that each of our clinical trials is conducted in accordance with applicable protocols, rules and regulations or in accordance with the general investigational plan and protocols for the trial as well as the various rules and regulations governing clinical trials in the United States and abroad. Any failure by those parties to perform their duties effectively and on a timely basis could harm our ability to develop and commercialize new products, harm our business and subject us to potential liabilities.

Physicians and patients may not accept or use our products

Even if the FDA approves our product candidates, physicians and patients may not accept or use them. Acceptance and use of our products will depend upon a number of factors including:

- perceptions by members of the health care community, including physicians, about the safety and effectiveness of our products;
- cost-effectiveness of our products relative to competing products or treatments;
- actual or perceived benefits of competing products or treatments;
- physicians' comfort level and prior experience with and use of competing products or treatments;
- availability of reimbursement for our products from government or other healthcare payers; and
- effectiveness of marketing and distribution efforts by us and our licensees and distributors.

We may require additional licenses or be subject to expensive and uncertain patent litigation in order to sell our products

A number of pharmaceutical and biotechnology companies and research and academic institutions have developed technologies, filed patent applications or received patents on various technologies that may be related to our business. Some of these technologies, applications or patents may conflict with our technologies or patent applications. As is common in the pharmaceutical and biotech industry, from time to time we receive notices from third parties alleging various challenges to our patent rights. Such conflicts, if proven, could invalidate our issued patents, limit the scope of the patents, if any, that we may be able to obtain, result in the denial of our patent applications or block our rights to exploit our technology. If the United States Patent and Trademark Office ("USPTO"), or foreign patent agencies have issued or in the future issue patents to other companies that cover our activities, we may not be able to obtain licenses to these patents at a reasonable cost, or at all, or be able to develop or obtain alternative technology. If we do not obtain such licenses, we could encounter delays in or be precluded altogether from introducing products to the market. If we are required to obtain additional licenses from third parties for the sale by Inspire of AzaSite in the United States and Canada, we will be required to pay for such additional licenses from our existing cash under the terms of the $60 million in aggregate principal amount of non-convertible, non-recourse promissory notes due in 2019 (the "AzaSite Notes").

We may need to litigate in order to defend against claims of infringement by others, to enforce patents issued to us or to protect trade secrets or know-how owned or licensed by us. Litigation could result in substantial cost to and diversion of effort by us, which may harm our business, prospects, financial condition and results of operations. Such costs can be particularly harmful to companies such as ours, without significant existing revenue streams or cash resources. We have also agreed to indemnify our licensees against infringement claims by third parties related to our technology, which could result in additional litigation costs and liability for us. In

addition, our efforts to protect or defend our proprietary rights may not be successful or, even if successful, may result in substantial cost to us, thereby utilizing our limited resources for purposes other than product development and commercialization.

If our products, methods, processes and other technologies infringe the proprietary rights of other parties, we could incur substantial costs and we may have to:

- obtain licenses, which may not be available on commercially reasonable terms, if at all;
- redesign our products or processes to avoid infringement;
- stop using the subject matter claimed in the patents held by others, which could preclude us from commercializing our products;
- pay damages; or
- defend litigation or administrative proceedings, which may be costly whether we win or lose, and which could result in a substantial diversion of our valuable management resources.

Our business depends upon our proprietary rights and we may not be able to protect, enforce, or secure our intellectual property rights adequately

Our future success will depend in large part on our ability to obtain patents, protect trade secrets, obtain and maintain rights to technology developed by others, and operate without infringing upon the proprietary rights of others. A substantial number of patents in the field of ophthalmology and genetics have been issued to pharmaceutical, biotechnology and biopharmaceutical companies. Moreover, competitors may have filed patent applications, may have been issued patents or may obtain additional patents and proprietary rights relating to products or processes competitive with ours. Our patent applications may not be approved. We may not be able to develop additional proprietary products that are patentable. Even if we receive patent issuances, those issued patents may not be able to provide us with adequate protection for our inventions or may be challenged by others.

A patent interference was declared before the Board of Patent Appeals and Interferences on certain U.S. patents covering AzaSite. Regents of the University of California assert that the inventions contained in these patents were made by a former employee of the university alone, and without collaboration with InSite Vision. They are asserting that they own those inventions, and that they are entitled to an award of priority of invention and a judgment that the inventions are not patentable to InSite Vision. InSite Vision believes the University's assertions are without merit and intends to vigorously contest those assertions. A declaration and adverse outcome of this interference would impact our royalty stream from Inspire for AzaSite.

Furthermore, the patents of others may impair our ability to commercialize our products. The patent positions of firms in the pharmaceutical and genetic industries generally are highly uncertain, involve complex legal and factual questions, and have recently been the subject of significant litigation. The USPTO and the courts have not developed, formulated, or presented a consistent policy regarding the breadth of claims allowed or the degree of protection afforded under pharmaceutical and genetic patents. Despite our efforts to protect our proprietary rights, others may independently develop similar products, duplicate any of our products or design around any of our patents. In addition, third parties from whom we have licensed or otherwise obtained technology may attempt to terminate or scale back our rights.

We also depend upon unpatented trade secrets to maintain our competitive position. Others may independently develop substantially equivalent proprietary information and techniques or otherwise gain access to our trade secrets. Our trade secrets may also be disclosed, and we may not be able to protect our rights to unpatented trade secrets effectively. To the extent that we, our consultants or our research collaborators use intellectual property owned by others, disputes also may arise as to the rights in related or resulting know-how and inventions.

In certain circumstances, we may lose the potential to receive future royalty payments after the AzaSite Notes are repaid in full or we may be required to pay damages for breaches of representations, warranties or covenants under certain of the AzaSite Note Financing Agreements

In February 2008, through a wholly-owned subsidiary, we issued $60 million in aggregate principal amount of AzaSite Notes, which are secured principally by royalty payments from future sales of AzaSite in North America, but not the right to receive such payments and by a pledge by us of all the outstanding equity interest in our subsidiary. If the AzaSite royalty payments are insufficient to repay the AzaSite Notes or if an event of default occurs under the indenture governing the AzaSite Notes, in certain circumstances, we would have to make payments on the AzaSite Notes out of our own cash resources, the royalty payments and our equity interest in our subsidiary may be foreclosed upon and we would lose the potential to receive future royalty payments after the AzaSite Notes are repaid in full and our intellectual property and other rights related to AzaSite. In addition, in connection with the issuance of the AzaSite Notes, we have made certain representations, warranties and covenants to our subsidiary and the holders of the AzaSite Notes (the "Noteholders"). If we breach these representations, warranties or covenants, such breach could trigger an event of default under the indenture and we could also be liable to our subsidiary or the Noteholders for substantial damages in respect of any such breach, which could harm our financial condition and ability to conduct our business as currently planned. See Note 6 of the Consolidated Financial Statements in this Annual Report on Form 10-K for a more complete description of the terms of the AzaSite Notes.

Inspire's failure to successfully market and commercialize AzaSite would harm sales of AzaSite and, therefore, would delay or prevent repayment of the AzaSite Notes, which would delay or prevent us from receiving future revenue from sales of AzaSite

The AzaSite Notes issued by our subsidiary will be repaid solely from royalties on net sales of AzaSite in the United States and Canada by Inspire under the Inspire License Agreement. Inspire has assumed full control of all promotional, sales and marketing activities for AzaSite in these territories, and has sole control over the pricing of AzaSite. Accordingly, royalty payments in respect of net sales of AzaSite in the United States and Canada, if Inspire markets AzaSite in Canada, will be entirely dependent on the actions, efforts and success of Inspire, over whom neither we nor our subsidiary have control. The success of Inspire's commercialization of AzaSite and the timely repayment of the AzaSite Notes will depend on a number of factors, including:

- the scope of Inspire's launch of AzaSite in the United States and Canada;
- the effectiveness and extent of Inspire's promotional, sales and marketing efforts;
- Inspire's ability to become and remain a viable ophthalmic company with sufficient operating resources;
- Inspire's ability to build, train and retain an effective sales force;
- Inspire's marketing efforts outside of the eye care professionals;
- Inspire's ability to successfully market AzaSite to physicians and patients;
- Inspire's pricing decisions regarding AzaSite;
- Inspire's marketing and selling of any current or future competing products;
- Inspire's ability to compete against larger and more experienced competitors;
- the discovery of any side effects or negative efficacy findings for AzaSite;
- product recalls or product liability claims relating to AzaSite;
- the introduction of generic competition;
- competing products for the treatment of bacterial conjunctivitis obtain more favorable formulary status than AzaSite; and
- the relevant parties' ability to adequately maintain or enforce the intellectual property rights relevant to AzaSite.

Inspire recently announced negative results in one of its key clinical trials and has limited financial resources. Inspire may determine to focus its resources on its internal development and other activities, which may harm Inspire's successful marketing of AzaSite and therefore impact our royalty payments.

Inspire has reported that it has incurred substantial expenses in establishing and maintaining its sales force for AzaSite, including substantial additional expenses for the training and management of personnel and the acquisition of infrastructure to enable its sales force to be effective and compliant with the multiple laws and regulations affecting sales and promotion of pharmaceutical products. Although individual members of the sales force have experience in sales with other companies, Inspire did not have a sales force prior to 2004 and may experience difficulties building and maintaining its sales force, which could harm sales of AzaSite.

Inspire is currently promoting AzaSite solely to eye care professionals. Pediatricians and primary care physicians write more than 67% of prescriptions for ophthalmic antibiotics. However, Inspire has no experience calling on pediatricians and primary care physicians. Inspire's focus on eye care professionals rather than pediatricians and primary care providers could result in lower AzaSite sales and therefore lower royalties paid to us. A large number of pharmaceutical companies, including those with competing products, much larger sales forces and much greater financial resources, and those with products for indications that are completely unrelated to AzaSite, compete for the time and attention of eye care professionals, pediatricians and primary care physicians. Neither we nor our subsidiary have any control over how Inspire manages and operates its sales force, how effective Inspire's sales efforts will be or Inspire's pricing decisions regarding AzaSite.

In addition, Inspire depends on three pharmaceutical wholesalers for the vast majority of its AzaSite sales in the United States. These companies are Cardinal Health, McKesson Corporation and AmerisourceBergen. The loss of any of these wholesalers could harm sales of AzaSite. It is also possible that these wholesalers, or others, could decide to change their policies or fees, or both, in the future. This could cause Inspire to incur higher product distribution costs, which would result in lower net sales of AzaSite.

Inspire could experience financial or other difficulties unrelated to AzaSite that could adversely affect the marketing or sale of AzaSite. Moreover, Inspire could change its commercial strategy and deemphasize or sell or sublicense its rights to AzaSite. Neither we nor our subsidiary can prevent Inspire from developing or licensing a product that competes with AzaSite or limiting or withdrawing its support of AzaSite. Our subsidiary's ability to pay amounts due on the AzaSite Notes may be materially harmed to the extent Inspire fails or is unable to successfully market and sell AzaSite. To the extent that our subsidiary fails to meet its payment obligations, we will have to make such payments out of our own cash resources in order to avoid a default under the AzaSite Notes, which we have done in the past. Our subsidiary again received insufficient royalties to make the interest payment in full that is due on February 15, 2011. We have the ability to make-up this shortfall with our own cash resources. This shortfall in interest payments constitutes a default under the indenture but not an event of default. To the extent that we pay in full the February 15th shortfall (plus interest thereon) by May 15, 2011, we will avoid triggering an event of default under the indenture. To the extent that an event of default occurs, the bondholders could seek available remedies, including foreclosure on our subsidiary. Our ability to receive future revenue from sales of AzaSite is dependent on our subsidiary repaying the AzaSite Notes in a timely fashion. If our subsidiary takes longer than anticipated to repay the AzaSite Notes, or if it defaults on the AzaSite Notes, we may not receive future revenue from AzaSite as currently planned, or at all.

Royalties under the Inspire License Agreement may not be sufficient for our subsidiary to meet its payment obligations under the AzaSite Notes

Inspire's obligation to pay royalties on net sales of AzaSite under the Inspire License Agreement expires on a country-by-country basis upon the later of 11 years from the first commercial sale of AzaSite or when the last valid claim under one of our licensed patents covering a subject product under the Inspire License Agreement in the United States and Canada expires. In the United States, first commercial sales occurred in August 2007, therefore, the obligation to pay royalties expires in August 2018. While our subsidiary will be entitled to

minimum royalties under the Inspire License Agreement from Inspire for five years after the first year of a commercial sale, such minimum royalties will not be sufficient for our subsidiary to meet its payment obligations under the AzaSite Notes and, therefore, it will be dependent on Inspire's successful sales and marketing efforts for AzaSite in order for it to receive royalties in excess of these minimum amounts. To the extent that royalties, including minimum royalties, are insufficient for our subsidiary to meet its payment obligations, we will have to make such payments out of our own cash resources in order to avoid a default under the notes, which we have done in the past. In addition, Inspire's obligation to pay minimum royalties is suspended during any period in which (i) the FDA or any other applicable regulatory authority has required any Inspire licensed product to be withdrawn from the market or the marketing thereof otherwise to be suspended in the United States or (ii) Inspire is unable, despite use of commercially reasonable efforts, to obtain supply of any Inspire licensed product in finished form in commercially reasonable amounts necessary to launch or market such Inspire licensed product in the United States.

Royalties under the Inspire License Agreement are subject to a cumulative reduction or offset in the event of patent invalidity, generic competition, uncured material breaches by us or in the event that Inspire is required to pay royalties, milestone payments or license fees to third parties for the continued use of AzaSite. The applicable royalty rate is also subject to reduction by up to 50% in any country during any period in which AzaSite does not have patent protection. These cumulative reductions or offsets could result in our subsidiary receiving significantly reduced or no royalties under the Inspire License Agreement, which would delay repayment of the AzaSite Notes, or result in a default under the AzaSite Notes. In such circumstances we may not receive future revenue from AzaSite as currently planned, or at all.

If the Inspire License Agreement is terminated in whole or in part while the AzaSite Notes remain outstanding, we will be forced to find a new third party collaborator for AzaSite, pursue commercialization efforts ourselves or else we will lose our right to certain intellectual property rights related to AzaSite to our subsidiary

In February 2008, in connection with our subsidiary's issuance of the AzaSite Notes, we entered into the residual license agreement with our subsidiary (the "Residual License Agreement"). Under the terms of the Residual License Agreement, if the Inspire License Agreement is terminated in the United States or Canada while the AzaSite Notes are outstanding, all of our rights to AzaSite in such country or countries will be licensed to our subsidiary and we have three months under the terms of the Interim Sublicense, which is a part of the Residual License Agreement, to find a new third party collaborator to undertake commercialization efforts with respect to AzaSite or pursue commercialization efforts ourselves in such country or countries. Inspire can terminate the Inspire License Agreement unilaterally in a variety of circumstances, including at any time in its discretion. If the Inspire License Agreement is terminated, our efforts to find a new third-party collaborator or pursue direct commercialization efforts ourselves will divert the attention of senior management from our current business operations, which could delay the development or licensing of our other product candidates. If we elect to commercialize AzaSite ourselves, we may expend significant resources as we currently have no sales, marketing or distribution capabilities or experience, and have no current plans to establish any such resources, which may not be successful and could harm our financial condition and results of operation.

If we are unsuccessful in finding a new third party collaborator for AzaSite or elect not to pursue commercialization efforts ourselves, the Interim Sublicense will terminate and our subsidiary will retain all rights to the intellectual property with respect to AzaSite in the related country or countries in which the Inspire License Agreement was terminated. If the Interim Sublicense terminates in accordance with the Residual License Agreement, our subsidiary may grant a sublicense under the license granted under the Residual License Agreement or pursue commercialization efforts itself. In any such circumstances, our subsidiary will remit for payment on the AzaSite Notes any royalties and other payments arising from the exercise of the license under the Residual License Agreement. As all economic value arising from the intellectual property subject to the Inspire License Agreement shall remain with our subsidiary (whether or not the Inspire License Agreement remains in effect and whether or not our subsidiary continues to be owned by us or our equity in the subsidiary is foreclosed upon by the Noteholders),

while the AzaSite Notes are outstanding and following repayment thereof, we may never receive any future royalties or economic benefit from AzaSite and may lose rights to the intellectual property relating thereto.

We rely on a sole source for the supply of the active pharmaceutical ingredient for AzaSite

We currently have a single supplier for azithromycin, the active drug incorporated into AzaSite. Under the Inspire License Agreement and the Supply Agreement, we have agreed to provide a supply of azithromycin to Inspire for the manufacture of AzaSite in the Territory, which we currently arrange through one supplier. The supplier of azithromycin has a drug master file on the compound with the FDA and is subject to the FDA's review and oversight. The supplier's manufacturing facility is subject to potential natural disasters, including earthquakes, hurricanes, tornadoes, floods, fires or explosions, and other interruptions in operation due to factors including labor unrest or strikes, failures of utility services or microbial or other contamination. If the supplier failed or refused to continue to supply us, if the FDA were to identify issues in the production of azithromycin that the supplier was unable to resolve quickly and cost-effectively, or if other issues were to arise that impact production, Inspire's ability to manufacture and commercialize AzaSite could be interrupted, and our subsidiary's ability to pay amounts due on the AzaSite Notes may be materially harmed, which could force us to make such payments out of our own cash resources in order to avoid a default under the AzaSite Notes and prevent or delay our ability to receive future revenue from AzaSite. Additional suppliers for azithromycin exist, but qualification of an alternative source could be time consuming and expensive and, during such qualification process, could negatively impact the sales of AzaSite. There is also no guarantee that these additional suppliers can supply sufficient quantities or quality product at a reasonable price, or at all. While we are required to maintain a certain level of inventory of azithromycin to support Inspire's manufacturing needs, that inventory may not be sufficient to prevent an interruption in the availability of AzaSite.

In addition, certain of the raw materials that we use in formulating DuraSite, the drug delivery system used in AzaSite, are available only from Lubrizol Advanced Materials, Inc. ("Lubrizol"). Although we do not have a current supply agreement with Lubrizol, we have not encountered any difficulties obtaining necessary materials from Lubrizol. Any significant interruption in the supply of these raw materials could delay sales of AzaSite, which could then harm our subsidiary's ability to pay amounts due on the AzaSite Notes and affect our ability to receive future revenue from AzaSite.

We have to attract and retain key employees to be successful

A critical factor to our success will be retaining our personnel or recruiting replacement personnel. Competition for skilled individuals in the biotechnology business, particularly in the San Francisco Bay Area is highly competitive, and we may not be able to continue to attract and retain personnel necessary for the development of our business. Our ability to attract and retain such individuals may be reduced by our current financial situation and the challenges we face. Moreover, a significant portion of our outstanding stock options have exercise prices that are higher than our current trading price, which may reduce the retention benefit of such stock options. The loss of key personnel, the failure to recruit replacement personnel or to develop needed expertise would harm our business.

If we engage in acquisitions, we will incur a variety of costs and the anticipated benefits of the acquisitions may never be realized

In the future, we may pursue acquisitions of companies, product lines, technologies or businesses that our management believes may be complementary or otherwise beneficial to us. Any of these acquisitions, if completed, could have a negative effect on our business. Future acquisitions may result in substantial dilution to our stockholders, the expenditure of our current cash resources, the incurrence of additional debt and amortization expenses related to goodwill, research and development and other intangible assets. In addition, acquisitions would involve many risks for us, including:

- assimilating employees, operations, technologies and products from the acquired companies with our existing employees, operations, technologies and products;

- the potential need for additional funding to support our combined business;
- diverting our management's attention from day-to-day operation of our business;
- entering markets in which we have no or limited direct experience; and
- potentially losing key employees from the acquired companies.

If we fail to adequately manage these risks we may not achieve the intended benefits from our acquisitions.

We may need to raise additional funds in the future, which could be difficult to obtain or could dilute the value and rights of our common stock, and which if not obtained in satisfactory amounts may prevent us from developing our products, conducting clinical trials or otherwise taking advantage of future opportunities or growing our business, any of which could harm our business

We may need to raise additional funds through equity or public or private debt, and we cannot be certain that we will be able to obtain additional financing on favorable terms, if at all. The current worldwide financing environment is challenging, particularly for smaller capitalized businesses such as ours, which could make it more difficult for us to raise funds on reasonable terms, or at all. If we issue additional equity securities, our stockholders will experience dilution and the new equity securities may have rights, preferences or privileges senior to those of existing holders of common stock. If we raise funds through debt, we will have to pay interest and may be subject to restrictive covenants, which would restrict operating flexibility and could harm our business. If we cannot raise sufficient funds or achieve acceptable terms, if and when needed, we may not be able to develop our products, conduct clinical trials, have the financial strength and leverage to negotiate favorable terms with potential marketing partners, market our products, take advantage of future opportunities, grow our business or respond to competitive pressures or unanticipated industry changes, any of which could harm our business.

Our products are subject to government regulations and approvals which may delay or prevent the marketing of potential products and impose costly procedures upon our activities

The FDA and comparable agencies in state and local jurisdictions and in foreign countries impose substantial requirements upon preclinical and clinical testing, manufacturing and marketing of pharmaceutical products. Lengthy and detailed preclinical and clinical testing, validation of manufacturing and quality control processes, and other costly and time-consuming procedures are required. Satisfaction of these requirements typically takes several years and the time needed to satisfy them may vary substantially, based on the type, complexity and novelty of the pharmaceutical product. The effect of government regulation may be to delay or to prevent marketing of potential products for a considerable period of time and to impose costly procedures upon our activities. The FDA or any other regulatory agency may not grant approval on a timely basis, or at all, for any products we develop. Success in preclinical or early stage clinical trials does not assure success in later stage clinical trials. Data obtained from preclinical and clinical activities are susceptible to varying interpretations that could delay, limit or prevent regulatory approval. If regulatory approval of a product is granted, such approval may impose limitations on the indicated uses for which a product may be marketed. Further, even after we have obtained regulatory approval, later discovery of previously unknown problems with a product may result in restrictions on the product, including withdrawal of the product from the market. Moreover, the FDA has recently reduced previous restrictions on the marketing, sale and prescription of products for indications other than those specifically approved by the FDA. Accordingly, even if we receive FDA approval of a product for certain indicated uses, our competitors, including our collaborators, could market products for such indications even if such products have not been specifically approved for such indications. If the FDA determines regulatory approval is required, any delay in obtaining or failure to obtain regulatory approvals would make it difficult or impossible to market our products and would harm our business, prospects, financial condition, and results of operations.

The FDA's policies may change and additional government regulations may be promulgated which could prevent or delay regulatory approval of our potential products. Moreover, increased attention to the containment

of health care costs in the United States could result in new government regulations that could harm our business. Adverse governmental regulation might arise from future legislative or administrative action, either in the United States or abroad. See "Uncertainties regarding healthcare reform and third-party reimbursement may impair our ability to raise capital, form collaborations and sell our products."

We have no experience in commercial manufacturing and if contract manufacturing is not available to us or does not satisfy regulatory requirements, we will have to establish our own regulatory compliant manufacturing capability and may not have the financial resources to do so

We have no experience manufacturing products for Phase 3 and commercial purposes at our own facility. We have a pilot facility licensed by the State of California to manufacture a number of our products for Phase 1 and Phase 2 clinical trials but not for late stage clinical trials or commercial purposes. Any delays or difficulties that we may encounter in establishing and maintaining a relationship with qualified manufacturers to produce, package and distribute our products may harm our clinical trials, regulatory filings, market introduction and subsequent sales of our products.

Contract manufacturers must adhere to current Good Manufacturing Practices regulations that are strictly enforced by the FDA on an ongoing basis through the FDA's facilities inspection program. Contract manufacturing facilities must pass a pre-approval plant inspection before the FDA will approve an NDA. Some of the material manufacturing changes that occur after approval are also subject to FDA review and clearance or approval. While the FDA has approved the AzaSite manufacturing process and facility, the FDA or other regulatory agencies may not approve the process or the facilities by which any of our other products may be manufactured. Our dependence on third parties to manufacture our products may harm our ability to develop and deliver products on a timely and competitive basis. Should we be required to manufacture products ourselves, we:

- will be required to expend significant amounts of capital to install a manufacturing capability;
- will be subject to the regulatory requirements described above;
- will be subject to similar risks regarding delays or difficulties encountered in manufacturing any such products; and
- will require substantially more additional capital than we otherwise may require.

Therefore, we may not be able to manufacture any products successfully or in a cost-effective manner.

We compete in highly competitive markets and our competitors' financial, technical, marketing, manufacturing and human resources may surpass ours and limit our ability to develop and/or market our products and technologies

Our success depends upon developing and maintaining a competitive advantage in the development of products and technologies in our areas of focus. We have many competitors in the United States and abroad, including pharmaceutical, biotechnology and other companies with varying resources and degrees of concentration in the ophthalmic market. Our competitors may have existing products or products under development which may be technically superior to ours or which may be less costly or more acceptable to the market. Our competitors may obtain cost advantages, patent protection or other intellectual property rights that would block or limit our ability to develop our potential products. Competition from these companies is intense and is expected to increase as new products enter the market and new technologies become available. Many of our competitors have substantially greater financial, technical, marketing, manufacturing and human resources than we do, particularly in light of our current financial condition. In addition, they may succeed in developing technologies and products that are more effective, safer, less expensive or otherwise more commercially acceptable than any that we have or will develop. Our competitors may also obtain regulatory approval for commercialization of their products more effectively or rapidly than we will. If we decide to manufacture and market our products by ourselves, we will be competing in areas in which we have limited or no experience such as manufacturing efficiency and marketing capabilities.

If we cannot compete successfully for market share against other drug companies, we may not achieve sufficient product revenues and our business will suffer

The market for our product candidates is characterized by intense competition and rapid technological advances. If our product candidates receive FDA approval, they will compete with a number of existing and future drugs and therapies developed, manufactured and marketed by others. Existing or future competing products may provide greater therapeutic convenience or clinical or other benefits for a specific indication than our products or may offer comparable performance at a lower cost. If our products fail to capture and maintain market share, we may not achieve sufficient product revenues and our business will be harmed.

We will compete against fully integrated pharmaceutical companies and smaller companies that are collaborating with larger pharmaceutical companies, academic institutions, government agencies and other public and private research organizations. Many of these competitors have products competitive with AzaSite already approved or in development, including Zymar and Ocuflox by Allergan, Vigamox and Ciloxan by Alcon, and Quixin by Johnson & Johnson. In addition, many of these competitors, either alone or together with their collaborative partners, operate larger research and development programs and have substantially greater financial resources than we do, as well as significantly greater experience in:

- developing drugs;
- undertaking pre-clinical testing and human clinical trials;
- obtaining FDA and other regulatory approvals of drugs;
- formulating and manufacturing drugs;
- launching, marketing and selling drugs; and
- attracting qualified personnel, parties for acquisitions, joint ventures or other collaborations.

Uncertainties regarding healthcare reform and third-party reimbursement may impair our ability to raise capital, form collaborations and sell our products

The continuing efforts of governmental and third-party payers to contain or reduce the costs of healthcare through various means may harm our business. For example, in some foreign markets, the pricing or profitability of healthcare products is subject to government control. In the United States, there have been, and we expect there will continue to be, a number of federal and state proposals to implement similar government control. The implementation or even the announcement of any of these legislative or regulatory proposals or reforms could harm our business by reducing the prices we or our partners are able to charge for our products, impeding our ability to achieve profitability, raise capital or form collaborations. In addition, the availability of reimbursement from third-party payers determines, in large part, the demand for healthcare products in the United States and elsewhere. Examples of such third-party payers are government and private insurance plans. Significant uncertainty exists as to the reimbursement status of newly approved healthcare products and third-party payers are increasingly challenging the prices charged for medical products and services. If we or our partners succeed in bringing one or more products to the market, reimbursement from third-party payers may not be available or may not be sufficient to allow the sale of these products on a competitive or profitable basis.

Our insurance coverage may not adequately cover our potential product liability exposure

We are exposed to potential product liability risks inherent in the development, testing, manufacturing, marketing and sale of human therapeutic products. Product liability insurance for the pharmaceutical industry is expensive. Although we believe our current insurance coverage is adequate to cover likely claims we may encounter given our current stage of development and activities, our present product liability insurance coverage will not be adequate to cover all potential claims we may encounter, particularly as AzaSite is commercialized outside the United States and Canada. Once AzaSite is commercialized in other countries, we may have to increase our coverage, which will be expensive, and we may not be able to obtain or afford adequate insurance coverage against potential claims in sufficient amounts or at a reasonable cost.

Our use of hazardous materials may pose environmental risks and liabilities which may cause us to incur significant costs

Our research, development and manufacturing processes involve the controlled use of small amounts of hazardous solvents used in pharmaceutical development and manufacturing, including acetic acid, acetone, acrylic acid, calcium chloride, chloroform, dimethyl sulfoxide, ethyl alcohol, hydrogen chloride, nitric acid, phosphoric acid and other similar solvents. We retain a licensed outside contractor that specializes in the disposal of hazardous materials used in the biotechnology industry to properly dispose of these materials, but we cannot completely eliminate the risk of accidental contamination or injury from these materials. Our cost for the disposal services rendered by our outside contractor was not material for the years ended 2010, 2009, or 2008, respectively. In the event of an accident involving these materials, we could be held liable for any damages that result and any such liability could exceed our resources. Moreover, as our business develops we may be required to incur significant costs to comply with federal, state and local environmental laws, regulations and policies, especially to the extent that we manufacture our own products.

Management and principal stockholders may be able to exert significant control on matters requiring approval by our stockholders

As of December 31, 2010, our management and principal stockholders (those owning more than 5% of our outstanding shares) together beneficially owned approximately 27% of our shares of common stock. As a result, our management and principal stockholders, acting together or individually, may be able to exert significant control on matters requiring approval by our stockholders, including the election of all or at least a majority of our Board of Directors, the approval of amendments to our charter, and the approval of business combinations and certain financing transactions. In September 2008, a group of our stockholders prevailed in a proxy contest that resulted in the replacement of all members of our Board of Directors.

The market prices for securities of biopharmaceutical and biotechnology companies such as ours have been and are likely to continue to be highly volatile due to reasons that are related and unrelated to our operating performance and progress; we have not paid dividends in the past and do not anticipate doing so in the future

The market prices for securities of biopharmaceutical and biotechnology companies, including ours, have been highly volatile. The market has from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. In addition, future announcements and circumstances, the status of our relationships or proposed relationships with third-party collaborators, the results of testing and clinical trials, future sales of equity or debt securities by us, the exercise of outstanding options and warrants that could result in dilution to our current holders of common stock, developments in our patents or other proprietary rights or those of our competitors, our own or Inspire's failure to meet analyst expectations, any litigation regarding the same, technological innovations or new therapeutic products, governmental regulation, or public concern as to the safety of products developed by us or others and general market conditions concerning us, our competitors or other biopharmaceutical companies may have a significant effect on the market price of our common stock. For example, in the twelve months ended December 31, 2010, our closing stock price fluctuated from a high of $0.57 to a low of $0.25. Such fluctuations can lead to securities class action litigation. Securities litigation against us could result in substantial costs and a diversion of our management's attention and resources, which could have an adverse effect on our business.

We have not paid any cash dividends on our common stock and we do not anticipate paying any dividends on our common stock in the foreseeable future.

Our common stock was delisted from the New York Stock Exchange Alternext US

On April 21, 2009, our common stock was delisted from the NYSE Alternext US LLC (the "Exchange") for our failure to comply with the Exchange's stockholders equity requirements. Our common stock currently trades

on the over-the-counter bulletin board ("OTCBB") market, although there are no assurances that it will continue to trade on this market. OTC transactions involve risks in addition to those associated with transactions on a stock exchange. The delisting and OTC status could harm the trading volume and liquidity of our common stock and, as a result, the market price for our common stock might become more volatile. The delisting and OTC status could also cause a reduction in the number of investors willing or able to hold or acquire our common stock, transactions in our common stock could be delayed and securities analysts' and news media coverage of us may be reduced. These factors could result in lower prices and larger spreads in the bid and ask prices for shares of common stock. Delisting and OTC status could also make our common stock substantially less attractive as collateral for loans, for investment by potential financing sources under their internal policies or state and federal securities laws or as consideration in future capital raising transactions. Furthermore, the delisting and OTC status may have other negative implications, including the potential loss of confidence by suppliers, partners and employees. Our OTC status may also make it more difficult and expensive for us to comply with state and federal securities laws in connection with future financings, acquisitions or equity issuances to employees and other service providers, thereby making it more difficult and expensive for us to raise capital, acquire other businesses using our stock and compensate our employees using equity.

We have adopted and are subject to anti-takeover provisions that could delay or prevent an acquisition of our Company and could prevent or make it more difficult to replace or remove current management

Provisions of our certificate of incorporation and bylaws may constrain or discourage a third party from acquiring or attempting to acquire control of us. Such provisions could limit the price that investors might be willing to pay in the future for shares of our common stock. In addition, such provisions could also prevent or make it more difficult for our stockholders to replace or remove current management and could adversely affect the price of our common stock if they are viewed as discouraging takeover attempts, business combinations or management changes that stockholders consider in their best interest. Our Board of Directors has the authority to issue up to 5,000,000 shares of our preferred stock (the "Preferred Stock"). Our Board of Directors has the authority to determine the price, rights, preferences, privileges and restrictions, including voting rights, of the unissued shares of Preferred Stock without any further vote or action by the stockholders. The rights of the holders of common stock will be subject to, and may be adversely affected by, the rights of the holders of any Preferred Stock that may be issued in the future. The issuance of Preferred Stock, while providing desirable flexibility in connection with possible financings, acquisitions and other corporate purposes, could have the effect of making it more difficult for a third party to acquire a majority of our outstanding voting stock, even if the transaction might be desired by our stockholders. Provisions of Delaware law applicable to us could also delay or make more difficult a merger, tender offer or proxy contest involving us, including Section 203 of the Delaware General Corporation Law, which prohibits a Delaware corporation from engaging in any business combination with any interested stockholder for a period of three years unless conditions set forth in the Delaware General Corporation Law are met. The issuance of Preferred Stock or Section 203 of the Delaware General Corporation Law could also be deemed to benefit incumbent management to the extent that these provisions deter offers by persons who would wish to make changes in management or exercise control over management. Other provisions of our certificate of incorporation and bylaws may also have the effect of delaying, deterring or preventing a takeover attempt or management changes that our stockholders might consider in their best interest. For example, our bylaws limit the ability of stockholders to remove directors and fill vacancies on our Board of Directors. Our bylaws also impose advance notice requirements for stockholder proposals and nominations of directors and prohibit stockholders from calling special meetings or acting by written consent.

If earthquakes and other catastrophic events strike, our business may be negatively affected

Our corporate headquarters, including our research and development and pilot plant operations, are located in the San Francisco Bay area, a region known for seismic activity. A significant natural disaster such as an earthquake would have a material adverse impact on our business, results of operations, and financial condition. If we were able to use the equipment at our contract manufacturing site we could conduct our pilot plant operations although we would incur significant additional costs and delays in our product development timelines.

We face the risk of a decrease in our cash balances and losses in our investment portfolio

Our investment policy is structured to limit credit risk and manage interest rate risk. By policy, we only invest in what we view as very high quality debt securities, such as United States Government securities. However, the recent uncertainties in the credit markets could prevent us from liquidating our positions in securities that we currently believe constitute high quality investments and could also result in the loss of some or all of our principal if the issuer of such securities defaults on its credit obligations. Following completion of our $60.0 million financing on February 21, 2008, investment income has become a more substantial component of our income. The ability to achieve our investment objectives is affected by many factors, some of which are beyond our control. Our interest income will be affected by changes in interest rates, which are highly sensitive to many factors, including governmental monetary policies and domestic and international economic and political conditions. The outlook for our investment income is dependent on the future direction of interest rates and the amount of cash flows from operations, if any, that are available for investment. Any significant decline in our investment income or the value of our investments as a result of falling interest rates, deterioration in the credit of the securities in which we have invested or general market conditions, could harm our ability to liquidate our investments, our cash position and our income.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

We currently lease approximately 39,123 square feet of research laboratory and office space located in Alameda, California. The facility includes laboratories for formulation, analytical, microbiology, pharmacology, quality control and development as well as a pilot manufacturing plant. The lease expires on December 31, 2013, and may be renewed by us for an additional 5-year term. In October 2010, we subleased approximately 11,640 square feet of office space at our facility. The sublease expires on December 31, 2013. We believe our existing facilities will be suitable and adequate to meet our needs for the immediate future.

Item 3. Legal Proceedings

The Company is subject to various claims and legal actions during the ordinary course of its business. On November 30, 2009, a patent interference was declared before the Board of Patent Appeals and Interferences on certain U.S. patents covering AzaSite. Regents of the University of California assert that the inventions contained in these patents were made by a former employee of the university alone, and without collaboration with InSite Vision. They are asserting that they own those inventions, and that they are entitled to an award of priority of invention and a judgment that the inventions are not patentable to InSite Vision. InSite Vision believes the University's assertions are without merit and intends to vigorously contest those assertions.

We believe that there are currently no other claims or legal actions that would have a material adverse impact on our financial position, operations or potential performance.

Item 4. (Removed and Reserved).

PART II

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

Market Information

Since April 21, 2009, our common stock has traded on the Over-the-Counter Bulletin Board ("OTCBB") market under the symbol "INSV." Over-the-counter market quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions. From September 30, 2008 to April 20, 2009, our common stock traded on The New York Stock Exchange Alternext US under the symbol "ISV." From June 10, 1998 to September 29, 2008, our common stock was traded on The American Stock Exchange under the symbol "ISV". The New York Stock Exchange Euronext acquired the American Stock Exchange on September 30, 2008. From our initial public offering on October 18, 1993 until June 9, 1998, our common stock traded on The Nasdaq National Market under the symbol "INSV." Prior to our initial public offering, there was no public market for our common stock. The following table sets forth the high and low closing sales prices for our common stock as reported by the OTCBB or The New York Stock Exchange Alternext US for the periods indicated. These prices do not include retail mark-ups, mark-downs or commissions.

2010	High	Low
First Quarter	0.57	0.34
Second Quarter	0.42	0.30
Third Quarter	0.36	0.25
Fourth Quarter	0.37	0.28

2009	High	Low
First Quarter	0.26	0.15
Second Quarter	0.59	0.26
Third Quarter	0.44	0.34
Fourth Quarter	0.47	0.36

Dividends

We have never declared or paid dividends on our common stock and do not anticipate paying any cash dividends in the foreseeable future. It is the present policy of our Board of Directors to retain our earnings, if any, for the development of our business.

Other Information

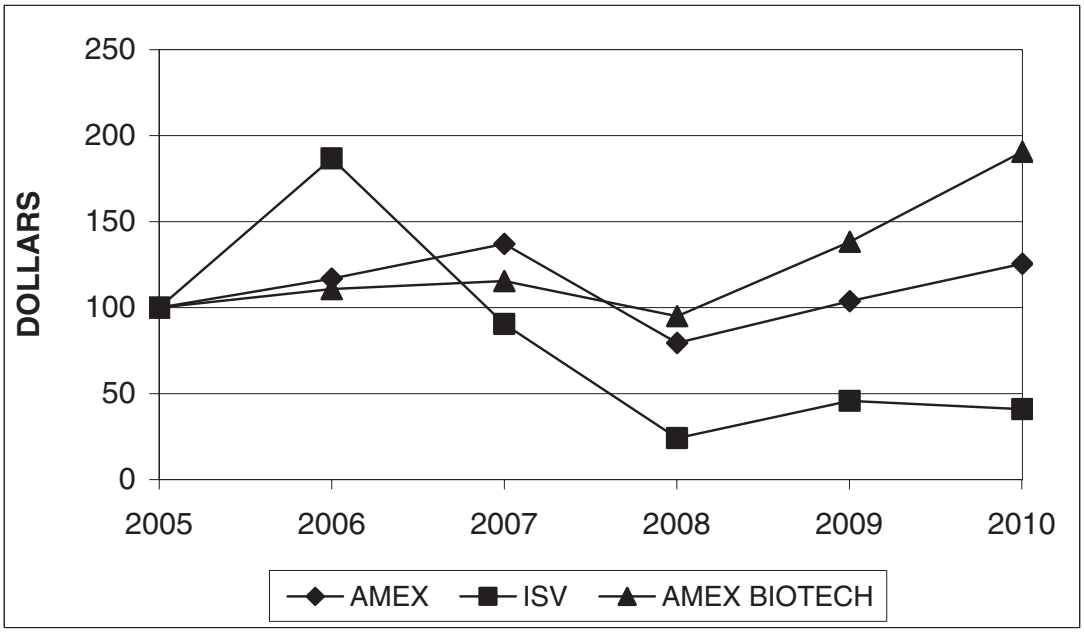
Information regarding employee stock-based compensation is provided in Note 10 in the Notes to the Consolidated Financial Statements in Item 8 of Part II of this Annual Report on Form 10-K. The remaining information required by this Item will be included in our Proxy Statement and such required information is incorporated herein by reference.

As of February 28, 2011, we had approximately 169 stockholders of record of our Common Stock. On February 28, 2011, the last sale price reported on the OTCBB for our common stock was $0.55 per share.

Stock Performance Graph

The following graph compares the percentage change in (i) the cumulative total stockholder return on our common stock from December 31, 2005 through December 31, 2010 with (ii) the cumulative total return on (a) the American Stock Exchange (U.S. Index) and (b) the American Stock Exchange (biotech) index. The comparison assumes (i) an investment of $100 on December 31, 2005 in each of the foregoing indices and (ii) reinvestment of dividends, if any.

The stock price performance shown on the graph below represents historical price performance and is not necessarily indicative of any future stock price performance.



	AMEX	ISV	AMEX BIOTECH
12/31/05	100	100	100
12/31/06	117	187	111
12/31/07	137	90	116
12/31/08	79	24	95
12/31/09	104	46	138
12/31/10	126	41	191

Notwithstanding anything to the contrary set forth in any of our previous filings under the Securities Act of 1933 or the Securities Exchange Act of 1934 which might incorporate any of our future filings made under those statutes, the preceding Stock Performance Graph will not be incorporated by reference into any of those prior filings, nor will such graph be incorporated by reference into any of our future filings made under those statues.

Recent Sales of Unregistered Securities

None.

Issuer Purchases of Securities

None.

Item 6. Selected Financial Data

The comparability of the following selected financial data is affected by a variety of factors, and this data is qualified by reference to and should be read in conjunction with the audited financial statements and notes thereto and the Management's Discussion and Analysis of Financial Condition and Results of Operations contained elsewhere in this Annual Report on Form 10-K. The following table sets forth selected financial data for us for the five years ended December 31, 2010 (in thousands except per share amounts):

	Year Ended December 31,				
(in thousands, except per share data)	**2010**	**2009**	**2008**	**2007**	**2006**
Statement of Operations Data					
Revenues:					
Royalties	$ 11,120	$ 8,000	$ 3,596	$ 701	$ —
Licensing fee, milestone amortization and other	747	1,798	10,110	23,060	2
Total revenues	11,867	9,798	13,706	23,761	2
Expenses:					
Research and development	4,974	5,436	16,242	10,384	8,890
General and administrative	4,511	5,792	8,251	6,760	6,182
Cost of revenues, principally royalties to third parties	1,727	1,549	630	982	28
Severance	—	527	1,909	—	—
Impairment of property and equipment	—	615	—	—	—
Total expenses	11,212	13,919	27,032	18,126	15,100
Interest expense and other, net	(10,248)	(10,034)	(7,984)	(100)	(1,513)
Net income (loss)	$ (9,593)	$ (14,155)	$ (21,310)	$ 5,535	$ (16,611)
Net income (loss) per share:					
Income (loss) per share—basic	$ (0.10)	$ (0.15)	$ (0.23)	$ 0.06	$ (0.19)
Income (loss) per share—diluted	$ (0.10)	$ (0.15)	$ (0.23)	$ 0.06	$ (0.19)
Weighted average shares used in per-share calculation:					
—Basic	94,774	94,710	94,607	94,168	88,339
—Diluted	94,774	94,710	94,607	100,110	88,339

	As of December 31,				
(in thousands)	**2010**	**2009**	**2008**	**2007**	**2006**
Balance Sheet Data:					
Cash, cash equivalents and short-term investments	$ 16,468	$ 24,721	$ 37,456	$ 11,532	$ 986
Working capital, exclusive of deferred revenues	14,104	22,816	35,068	9,589	(6,836)
Total assets	23,586	32,246	44,943	15,012	2,439
Non-recourse secured notes payable	60,000	60,000	60,000	—	—
Accumulated deficit	(192,585)	(182,992)	(168,837)	(147,527)	(153,062)
Total stockholders' equity (deficit)	$ (42,220)	$ (33,033)	$ (19,506)	$ 746	$ (6,302)

No cash dividends have been declared or paid by us since our inception.

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

The following discussion should be read in conjunction with the financial statements and notes thereto included in Item 8 of this Form 10-K.

Overview

We are an ophthalmic product development company advancing ophthalmic pharmaceutical products to address unmet eye care needs. Our current portfolio of products is based on our proprietary DuraSite® drug delivery technology.

Our DuraSite® sustained drug delivery technology is a proven synthetic polymer-based formulation designed to extend the residence time of a drug relative to conventional topical therapies. It enables topical delivery of a drug as a solution, gel or suspension and can be customized for delivering a wide variety of drug candidates. We have focused our research and development and commercial support efforts on the following topical products formulated with our DuraSite® drug delivery technology. We may also utilize our DuraSite technology platform for the formulation of new ocular product candidates using either non-proprietary drugs or compounds originally developed by others for non-ophthalmic indications.

- AzaSite® (azithromycin ophthalmic solution) 1% is a DuraSite formulation of azithromycin, a broad spectrum ocular antibiotic approved by the FDA in April 2007 to treat bacterial conjunctivitis (pink eye). It was launched in the United States by Inspire Pharmaceuticals in August 2007. Additional indications are being pursued by Inspire Pharmaceuticals for this product. The key advantages are a significantly reduced dosing regimen leading to better compliance and outcome, with a broad spectrum antibiotic, and a lowered probability of bacterial resistance based on high tissue concentration.
- Besivance™ (besifloxacin ophthalmic suspension) 0.6% is a DuraSite formulation of besifloxacin, a broad spectrum ocular antibiotic approved by the FDA in May 2009 to treat bacterial conjunctivitis (pink eye). An advantage of Besivance is a faster rate of resolution of the infection that may reduce the duration of the illness and reduce the chances of infecting others. Besivance was developed by Bausch & Lomb and launched in the United States in the second half of 2009.
- AzaSite Plus (ISV-502) is a fixed combination of azithromycin and dexamethasone in DuraSite for the treatment of ocular inflammation and infection (blepharitis and/or blepharoconjunctivitis) for which there is no FDA- approved indicated treatment; we completed the first Phase 3 trial in November 2008. AzaSite Plus was very well tolerated. However, the trial did not achieve its primary endpoint as defined by the protocol. We discussed the results of this trial with the FDA and determined a development plan for this product candidate. We are pursuing a Special Protocol Assessment ("SPA") for the next Phase 3 clinical trial for this product candidate.
- DexaSite (ISV-305) is a DuraSite formulation of dexamethasone in development for the treatment of ocular inflammation. We have met with the FDA to discuss the development pathway for this product candidate. We are pursuing an SPA for the next Phase 3 clinical trial for this product candidate.
- ISV-303 is a DuraSite formulation of bromfenac in development for the treatment of post-operative inflammation and eye pain. We initiated a Phase 1/2 clinical trial for this product candidate in August 2010 and completed patient enrollment in December 2010. We expect to have top-line results from this study in the first half of 2011. In addition, we anticipate an additional Phase 2 clinical trial to investigate the pharmacokinetics of ISV-303 in humans.
- ISV-101 is a DuraSite formulation with a low concentration of bromfenac for the treatment of dry eye disease. We filed an Investigational New Drug Application (IND) for this product candidate in the first quarter of 2011. We anticipate a Phase 1/2 clinical trial for this product candidate.

Major Developments and Events in 2010

Our major developments and events in 2010 included:

- meeting with the FDA to discuss the development pathway for AzaSite Plus, DexaSite and ISV-303;
- initiated and completed patient enrollment of a Phase 1/2 clinical trial for ISV-303,
- received $0.5 million in grants for the development of AzaSite Plus and ISV-303 from the Department of the Treasury under the Therapeutic Discovery Project under Section 48D of the Internal Revenue Code, and
- increased sales of AzaSite by Inspire in the United States.

Business Strategy

Our business strategy consists of the following:

1. **Develop our pipeline of ocular product candidates.** We identify new product candidates that consist of proven drugs that can be improved by formulation in DuraSite, which substantially reduces the clinical risk in these product candidates. We plan to conduct preclinical and clinical testing of our portfolio product candidates.
2. **Monetize our product candidates.** At the appropriate time, we seek to partner with larger pharmaceutical companies to complete the clinical development, manufacture and marketing of these products. Partnering agreements generally include upfront and milestone payments, as well as on-going royalty payments upon commercialization, for the Company.

Critical Accounting Policies and Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States requires us to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

We believe the following policies to be the most critical to an understanding of our financial condition and results of operations because they require us to make significant estimates, assumptions and judgments about matters that are uncertain:

Revenue Recognition. The Company's revenues are primarily related to royalties on product sales and licensing agreements, and such agreements may provide for various types of payments, including upfront payments, research funding and related fees during the term of the agreement, milestone payments based on the achievement of established development objectives, and licensing fees.

The Company recognizes revenue when four basic criteria are met: persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; the fee is fixed or determinable; and collectability is reasonably assured. The Company has arrangements with multiple elements. The Company analyzes its multiple element arrangements to determine whether the elements can be separated and accounted for individually as separate units of accounting. An item can generally be considered a separate unit of accounting if all of the following criteria are met: the delivered item(s) has value to the customer on a stand-alone basis; there is objective and reliable evidence of the fair value of the undelivered items(s); and if the arrangement includes a general right of return and delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Company. Items that cannot be divided into separate units are combined with other units of accounting, as appropriate. Consideration received is allocated among the separate units based on their respective fair values or based on the residual value method and is recognized in full when the criteria are met. The Company deems service to be rendered if no continuing obligation exists on the part of the Company.

The Company receives royalties from licensees based on third-party sales. The royalties are recorded as earned in accordance with the contract terms when third-party results are reliably measured and collectability is reasonably assured.

Revenue associated with non-refundable up-front license fees under arrangements where the license fees cannot be accounted for as separate units of accounting is deferred and recognized as revenue on a straight-line basis over the expected term of the Company's continued involvement. Revenues from the achievement of milestones, if deemed substantive, are recognized as revenue when the milestones are achieved, and the milestone payments are due and collectible. If not deemed substantive, the Company would recognize such milestone as revenue on a straight-line basis over the remaining expected term of continued involvement.

Milestones are considered substantive if all of the following conditions are met: the milestone is nonrefundable; achievement of the milestone was not reasonably assured at the inception of the arrangement; substantive effort is involved to achieve the milestone; and the amount of the milestone appears reasonable in relation to the effort expended, the other milestones in the arrangement and the related risk associated with the achievement of the milestone and any ongoing services are priced at fair value.

Income Taxes. Income tax expense has been provided using the liability method. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. The Company provides a valuation allowance against net deferred tax assets if, based upon the available evidence, it is not more likely than not that the deferred tax assets will be realized.

We file U.S. federal and California state income tax returns. To date, we have not been audited by the Internal Revenue Service or any state.

Our policy is to recognize interest and penalties related to the underpayment of income taxes as a component of income tax expense. To date, there have been no interest or penalties charged to us in relation to the underpayment of income taxes.

For the years ended December 31, 2010, 2009 and 2008, we generated net losses and, accordingly, did not record a provision for income taxes. As of December 31, 2010, our total deferred tax assets were $60.5 million. The deferred tax assets were primarily comprised of federal and state tax NOL carryforwards. Due to uncertainties surrounding our ability to continue to generate future taxable income to realize these tax assets, a full valuation allowance has been established to offset our deferred tax assets. Additionally, the future utilization of our NOL carryforwards to offset future taxable income is subject to an annual limitation as a result of ownership changes that have occurred previously and may be further impacted by future ownership changes. As necessary, the deferred tax assets have been reduced by any carryforwards that expire prior to utilization as a result of such limitations, with a corresponding reduction of the valuation allowance. These carryforwards may be further reduced if we have any additional ownership changes in the future.

Stock-Based Compensation. We granted stock-based awards to eligible employees and directors to purchase shares of our common stock under our stock compensation plan approved in 1994 (the 1994 Plan) and its successor the 2007 Performance Incentive Plan (the 2007 Plan). In addition, we have a qualified employee stock purchase plan (Purchase Plan) in which eligible employees may elect to withhold up to 15% of their compensation to purchase shares of our common stock on a quarterly basis at a discounted price equal to 85% of the lower of the employee's offering price or the closing price of the stock on the date of purchase. In August 2009, the Purchase Plan was suspended. The benefits provided by these plans qualify as stock-based compensation which requires us to recognize compensation expense based on their estimated fair values determined on the date of grant for all stock-based awards granted, modified or cancelled.

We estimate the fair value of share-based awards on the date of grant using the Black-Scholes option-pricing method (Black-Scholes method). The determination of fair value of share-based awards using an option-pricing model requires the use of certain estimates and assumptions that affect the reported amount of share-based compensation cost recognized in our Consolidated Statements of Income. These include estimates of the expected term of share-based awards, expected volatility of our stock price, expected dividends and the risk-free interest rate. These estimates and assumptions are highly subjective and may result in materially different amounts should circumstances change and we employ different assumptions in future periods.

For stock-based awards issued, we estimated the expected term by considering various factors including the vesting period of options granted and employees' historical exercise and post-employment termination behavior. Our estimated volatility was derived using our historical stock price volatility. We have never declared or paid any cash dividends on our common stock and currently do not anticipate paying such cash dividends. We currently anticipate that we will retain all of our future earnings for use in the development and expansion of our business and for general corporate purposes. Any determination to pay dividends in the future will be at the discretion of our Board of Directors and will depend upon our results of operations, financial condition, financial covenants, tax laws and other factors as the Board of Directors, in its discretion, deems relevant. The risk-free interest rate is based upon U.S. Treasury securities with remaining terms similar to the expected term of the stock-based awards.

Results of Operations

Revenues.

We had total revenues of $11.9 million, $9.8 million, and $13.7 million for the years ended December 31, 2010, 2009 and 2008, respectively.

In 2010, our revenues primarily consisted of $10.7 million of royalties from net sales of AzaSite by Inspire compared to $8.0 million in 2009. The $2.7 million increase in royalty revenues from the prior year was primarily due to a 22% increase of AzaSite net sales in the United States. In addition, the royalty rate for AzaSite increased from 20% to 25% in July 2009. 2010 revenues also included $0.5 million of royalties from net sales of Besivance by Bausch & Lomb, $0.5 million of grant income under the Therapeutic Discovery Program and $0.2 million from the sale of materials to Inspire under the Supply Agreement.

In 2009, our revenues primarily consisted of $8.0 million of royalties from net sales of AzaSite by Inspire compared to $3.6 million in 2008. The $4.4 million increase in royalty revenues from the prior year was primarily due to a 91% increase of AzaSite net sales and the royalty rate increase for AzaSite in July 2009. 2009 revenues also included $1.4 million of international AzaSite license fees. The remainder of our 2009 revenues represented sales of materials to Inspire under the Supply Agreement and contract services provided to Inspire related to their AzaSite activities.

In 2008, $9.9 million of our revenues represented the non-cash amortization of the license fee for AzaSite from Inspire. The amortization period for the license fee from Inspire for AzaSite ended in April 2008. 2008 revenues also included $3.6 million of royalties from net sales of AzaSite by Inspire. The remaining revenue in 2008 represented contract services provided to Inspire related to its AzaSite activities.

Research and development.

Our research and development activities can be separated into two major segments, research and clinical development. Research includes activities involved in evaluating a potential product, related preclinical testing and manufacturing. Clinical development includes activities related to filings with the FDA and the related human clinical testing required to obtain marketing approval for a potential product. We estimate that the following represents the approximate cost of these activities for 2010, 2009 and 2008 (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Research	$3,137	$4,407	$ 7,286
Clinical development	1,837	1,029	8,956
Total research and development	$4,974	$5,436	$16,242

Our research and development (R&D) expenses by program for 2010, 2009 and 2008 (in thousands) were:

Program	2010	2009	2008
ISV-303	$ 1.3	$ 0.2	$ —
AzaSite Plus	0.1	0.2	7.6
AzaSite	0.1	0.1	0.2
ISV-016	—	—	0.4
New products and other	0.6	0.1	0.9
Programs - non-specific	2.9	4.8	7.1
Total	$ 5.0	$ 5.4	$16.2

Research and development expenses were $5.0 million in 2010. In 2010, our program expenses primarily consisted of non-specific program costs which comprised facility, internal personnel and stock-based compensation costs that are not allocated to a specific development program. The non-specific costs decreased in 2010, as compared to 2009, primarily due to savings resulting from our corporate restructuring in March 2009. Our ISV-303 program expenses primarily related to preclinical experiments and the Phase 1/2 clinical trial that was initiated in August 2010.

Research and development expenses were $5.4 million in 2009. In 2009, our activities primarily consisted of non-specific program costs which comprised facility, internal personnel, and stock-based compensation costs that are not allocated to a specific development program. The non-specific costs decreased from 2008 due to our corporate restructuring which occurred in December 2008 and March 2009. Our AzaSite Plus program expenses in 2009 consisted primarily of ongoing consulting and data analysis pertaining to our Phase 3 clinical trial.

Research and development expenses were $16.2 million in 2008. In 2008, our activities primarily included the Phase 3 clinical trial of AzaSite Plus, preparation for the production of Canadian AzaSite registration batches at our contract manufacturing site, preclinical testing of AzaSite Otic, and preclinical experiments of ISV-405. Our activities related to the AzaSite Otic program were discontinued in July 2008 and our ISV-405 activities have been deferred.

Our future research and development expenses will depend on the results and magnitude or scope of our clinical, preclinical and research activities and requirements imposed by regulatory agencies. Accordingly, our research and development expense may fluctuate significantly from period to period. In addition, if we in-license or out-license rights to product candidates, our research and development expenses may fluctuate significantly from prior periods.

General and administrative.

General and administrative expenses decreased to $4.5 million in 2010 from $5.8 million in 2009. This decrease was primarily due to lower personnel-related expenses as a result of our March 2009 corporate restructuring.

General and administrative expenses decreased to $5.8 million in 2009 from $8.3 million in 2008. This decrease primarily reflected legal and other expenses related to our proxy contest in 2008. In addition, we incurred lower personnel-related expenses due to our December 2008 and March 2009 corporate restructuring.

Cost of revenues.

Our cost of revenues were $1.7 million, $1.5 million and $0.6 million for 2010, 2009 and 2008, respectively. Cost of revenues were primarily comprised of royalties accrued for third parties, including Pfizer, based on AzaSite net sales from Inspire. Cost of revenues also includes the cost of the azithromycin supplied to Inspire under the Supply Agreement.

Severance.

Severance expenses were $0.5 million and $1.9 million in 2009 and 2008, respectively, which were associated with our corporate restructuring which were announced in December 2008 and March 2009. No severance expense was incurred in 2010. As of December 31, 2010, the restructuring plan reduced our personnel by 39 employees.

Impairment of property and equipment.

Impairment expenses were $0.6 million in 2009 and were associated with our corporate restructuring announced in March 2009. The Company impaired laboratory and other equipment, leasehold improvements, and furniture and fixtures located at our corporate headquarters. No impairment expense was incurred in 2008 or 2010.

Interest expense and other, net.

Interest expense and other, net, was an expense of $10.2 million, $10.0 million and $8.0 million for 2010, 2009 and 2008, respectively. Interest expense was primarily due to the interest expense on the $60 million non-convertible, non-recourse promissory notes issued (the "AzaSite Notes") in February 2008 and related amortization of the debt issuance costs incurred from our issuance of the AzaSite Notes.

Liquidity and Capital Resources

In recent years, we have financed our operations primarily through private placements of equity securities, debt financings and payments from corporate collaborations. For the year ended December 31, 2008, we financed our operations primarily from the issuance of the AzaSite Notes. At December 31, 2010 and 2009, our cash, cash equivalents and short-term investments were $16.5 million and $24.7 million, respectively. It is our policy to invest our cash and cash equivalents in highly liquid securities, such as interest-bearing money market funds, treasury and federal agency notes. The current uncertain credit markets may affect the liquidity of such money market funds or other cash investments.

Cash used by operating activities was $8.1 million, $12.7 million and $29.5 million, for 2010, 2009 and 2008, respectively. In 2010, the decrease from 2009 primarily resulted from lower costs as a result of our corporate restructuring in 2009 and an increase in royalty revenue. In 2009, the decrease from 2008 primarily resulted from the $9.9 million of non-cash amortization of deferred revenue (license fee) from Inspire, $7.6 million of AzaSite Plus program expenses, $1.9 million of severance expenses and legal and other expenses related to our proxy contest that occurred in 2008.

Cash provided by investing activities was $12.4 million for 2010. Cash used in investing activities was $17.5 million and $0.5 million for 2009 and 2008, respectively. In 2009, the Company invested $17.5 million in short-term investments and converted $12.5 million back to cash and cash equivalents in 2010. In 2008, investing activities primarily related to cash outlays for additions to laboratory and other equipment.

Cash provided by financing activities was $16,000 for 2010. Cash used in financing activities was $7,000 for 2009. Cash provided by financing activities was $55.8 million for 2008, reflecting the net proceeds from the issuance of the AzaSite Notes.

The tables below set forth the amount of cash that we raised for fiscal years 2010 through 2008 from option exercises and stock purchases under our employee stock purchase plan, and debt financings.

Cash received from Option Exercises and Employee Stock Purchase Plans

Year	Net Proceeds
2010	$21,000
2009	$ 9,000
2008	$28,000

Cash Received from Private Placement of Notes

Date	Net Proceeds	Type of Notes	Interest Rates and Terms	Maturity Date
February 2008	$55.3 million	Long-Term Secured Notes	16% through May 15, 2019	May 15, 2019

In February 2008, our wholly-owned subsidiary, Azithromycin Royalty Sub, LLC completed a private placement of $60.0 million in aggregate principal amount of non-convertible, non-recourse secured promissory notes due in 2019. Net proceeds from the financing were approximately $55.3 million after transaction costs of approximately $4.7 million. In addition, $5.0 million of the proceeds was set aside for interest reserves. The annual interest rate on the notes is 16% with interest payable quarterly in arrears beginning May 15, 2008. The notes are secured by, and will be repaid from, royalties to be paid to us by Inspire Pharmaceuticals from sales of AzaSite in the United States and Canada. The secured notes payable are non-recourse to InSite Vision Incorporated. When the AzaSite royalties received for any quarter exceed the interest payments and certain expenses due that quarter, the excess will be applied to the repayment of principal of the notes until the notes have been paid in full. Any shortfall of interest payments from the royalty payments will be paid out of the interest reserves. As of December 31, 2010, no balance remained on the interest reserve. Further shortfalls, if any, may be paid by us at our option to avoid default under the agreement. The notes may be redeemed at our option, subject to the payment of a redemption premium through May 2012. As of December 31, 2010, the $60.0 million of secured notes payable is classified as long-term.

Our future capital expenditures and requirements will depend on numerous factors, including the progress of our clinical testing, research and development programs and preclinical testing, the time and costs involved in obtaining regulatory approvals, our ability to successfully commercialize any products that we may launch in the future, our ability to establish collaborative arrangements, the cost of filing, prosecuting, defending and enforcing patent claims and other intellectual property rights, competing technological and market developments, changes in our existing collaborative and licensing relationships, acquisition of new businesses, products and technologies, the completion of commercialization activities and arrangements, and the purchase of additional property and equipment.

We anticipate no material capital expenditures to be incurred for environmental compliance in fiscal year 2011. Based on our environmental compliance record to date, and our belief that we are current in compliance with applicable environmental laws and regulations, environmental compliance is not expected to have a material adverse effect on our operations.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect.

Contractual Obligations

The following table summarizes our significant contractual obligations as of December 31, 2010 and the effect such obligations are expected to have on our liquidity and cash flows in future periods. Some of these amounts are based on management's estimates and assumptions about these obligations including their duration, the possibility of renewal and other factors. Because these estimates are necessarily subjective, our actual payments in the future may vary from those listed in this table.

	Payments due by period (in thousands)				
	Total	Less than 1 year	1-3 years	3-5 Years	More than 5 years
Capital lease obligations (1)	$ 5	$ 5	$ —	$ —	$ —
Facilities lease obligations (2)	2,468	798	1,670	—	—
Licensing agreement obligations (3)	13,743	1,538	3,215	3,411	5,579
Secured notes payable (4)	60,000	1,503	15,035	7,584	35,878
Interest payments on secured notes payable (5)	60,264	11,959	17,750	13,369	17,186
Total commitments	$136,480	$15,803	$37,670	$24,364	$58,643

(1) We lease our telephones and telephone equipment under two capital lease agreements which expire in 2011.
(2) We lease our facilities under a non-cancelable operating lease that expires in 2013.
(3) We have entered into certain license agreements that require us to make royalty payments for the life of the licensed patents. The estimated royalties due under certain of these agreements are as noted for 2011 through 2019.
(4) Principal repayments are limited to royalties received from Inspire Pharmaceutical from sales of AzaSite in the United States and Canada. When the AzaSite royalties received for any quarter exceed the interest payments and certain expenses due that quarter, the excess will be applied to the repayment of principal of the notes until the notes have been paid in full. Future payments represent an estimate of expected principal repayments based on minimum royalty income covered by the agreement and future projected sales. The note is due in 2019.
(5) Interest repayments represent an estimate based on expected principal repayments.

Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board ("FASB") issued an amendment to accounting standards related to multiple-deliverable revenue arrangements. The amendment requires entities to allocate revenue in multiple-deliverable revenue arrangements using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The amendments eliminate the residual method of revenue allocation and require revenue to be allocated using the relative selling price method. The standard is effective on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning after June 15, 2010. The Company is currently evaluating the impact to the Company's financial position and results of operations.

In January 2010, the FASB issued an amendment to accounting standards related to fair value disclosures. The amendment requires entities to provide enhanced disclosures about transfers into and out of the Level 1 (fair value determined based on quoted prices in active markets for identical assets and liabilities) and Level 2 (fair value determined based on significant other observable inputs) classifications, provide separate disclosure about purchases, sales, issuances and settlements relating to the tabular reconciliation of beginning and ending balances of the Level 3 (fair value determined based on significant unobservable inputs) classification and provide greater disaggregation for each class of assets and liabilities that use fair value measurements. The standard is effective for interim and annual reporting periods beginning after December 31, 2009, except for the Level 3 disclosure. The Company adopted this standard during the period ended March 31, 2010. The adoption did not impact the

Company's consolidated financial position or results of operations. The Level 3 disclosure is effective for interim and annual reporting periods beginning after December 31, 2010. The Company expects that the adoption of the Level 3 disclosure will not materially impact the Company's consolidated financial position or results of operations, other than additional disclosure requirements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The following discusses our exposure to market risk related to changes in interest rates.

We have long-term debt with fixed interest rates. As a result, our exposure to market risk caused by fluctuations in interest rates is minimal. Our borrowings outstanding as of December 31, 2010 were $60 million and the interest rate was 16%. If the market interest rates increased by 10% from the December 31, 2010 levels, it would not result in an increase in interest expense. As of December 31, 2010, the face value of our long-term debt was estimated to be approximately the fair value based on current market rates.

The securities in our investment portfolio are not leveraged and are subject to minimal interest rate risk. Due to their original maturities of twelve months or less, the securities are classified as cash and cash equivalents or short-term investments. They are classified as trading securities principally bought and held for the purpose of selling them in the near term, with unrealized gains and losses included in earnings. Because of the short-term maturities of our investments, we do not believe that a change in market rates would have a significant negative impact on the value of our investment portfolio. While a hypothetical decrease in market interest rates by 10 percent from the December 31, 2010 levels would cause a decrease in interest income, it would not result in loss of principal.

The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. To achieve this objective in the current economic environment, we maintain our portfolio in cash equivalents or short-term investments, including obligations of United States government-sponsored enterprises and money market funds. These securities are classified as cash and cash equivalents or short-term investments and consequently are recorded on the balance sheet at fair value. We do not utilize derivative financial instruments to manage our interest rate risks.

Item 8. Financial Statements and Supplementary Data

The following Consolidated Financial Statements and Report of Independent Registered Public Accounting Firm are included on the pages that follow:

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders of
InSite Vision Incorporated

We have audited the accompanying consolidated balance sheets of InSite Vision Incorporated and subsidiaries (the "Company") as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholders' equity (deficit), and cash flows for each of the three years in the period ended December 31, 2010. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor have we been engaged to perform, an audit of the Company's internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of InSite Vision Incorporated as of December 31, 2010 and 2009, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2010, in conformity with accounting principles generally accepted in the United States of America.

/s/ Burr Pilger Mayer, Inc.

San Francisco, California
March 4, 2011

INSITE VISION INCORPORATED

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)	December 31, 2010	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 11,469	$ 7,222
Short-term investments	4,999	17,499
Accounts receivable, net	3,352	3,137
Prepaid expenses and other current assets	15	157
Total current assets	19,835	28,015
Property and equipment, net	247	309
Debt issuance costs, net	3,504	3,922
Total assets	$ 23,586	$ 32,246
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Current liabilities:		
Accounts payable	$ 332	$ 286
Accrued liabilities	511	360
Accrued compensation and related expense	620	968
Accrued royalties	892	647
Accrued interest	3,376	2,938
Deferred revenues	75	75
Total current liabilities	5,806	5,274
Capital lease obligation, less current portion	—	5
Non-recourse secured notes payable	60,000	60,000
Total liabilities	65,806	65,279
Commitments and contingencies		
Stockholders' deficit:		
Preferred stock, $0.01 par value, 5,000,000 shares authorized, none issued and outstanding	—	—
Common stock, $0.01 par value, 240,000,000 shares authorized; 94,822,593 and 94,738,400 shares issued and outstanding at December 31, 2010 and 2009, respectively	948	947
Additional paid-in capital	149,417	149,012
Accumulated deficit	(192,585)	(182,992)
Total stockholders' deficit	(42,220)	(33,033)
Total liabilities and stockholders' deficit	$ 23,586	$ 32,246

See accompanying notes to consolidated financial statements.

INSITE VISION INCORPORATED

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)	Year Ended December 31, 2010	2009	2008
Revenues:			
Royalties	$ 11,120	$ 8,000	$ 3,596
Licensing fee and milestone amortization	—	1,423	9,972
Other product and service revenues	747	375	138
Total revenues	11,867	9,798	13,706
Expenses:			
Research and development (a)	4,974	5,436	16,242
General and administrative (a)	4,511	5,792	8,251
Cost of revenues, principally royalties to third parties	1,727	1,549	630
Severance	—	527	1,909
Impairment of property and equipment	—	615	—
Total expenses	11,212	13,919	27,032
Income (loss) from operations	655	(4,121)	(13,326)
Interest expense and other, net	(10,248)	(10,034)	(7,984)
Net loss	$ (9,593)	$(14,155)	$(21,310)
Net loss per share:			
Loss per share—basic	$ (0.10)	$ (0.15)	$ (0.23)
Loss per share—diluted	$ (0.10)	$ (0.15)	$ (0.23)
Weighted average shares used in per-share calculation:			
—Basic	94,774	94,710	94,607
—Diluted	94,774	94,710	94,607
(a) Stock-based compensation included in expense line items:			
Research and development	$ 74	$ 319	$ 290
General and administrative	311	300	740

See accompanying notes to consolidated financial statements.

INSITE VISION INCORPORATED

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)

(in thousands, except share data)	Common Stock Shares	Common Stock Amount	Additional Paid-in-Capital	Accumulated Deficit	Total Stockholders' Equity (Deficit)
Balances, December 31, 2007	94,585,449	$946	$147,327	$(147,527)	$ 746
Issuance of common stock from employee stock purchase plan	96,169	1	27	—	28
Stock-based compensation	—	—	1,030	—	1,030
Net loss	—	—	—	(21,310)	(21,310)
Balances, December 31, 2008	94,681,618	947	148,384	(168,837)	(19,506)
Issuance of common stock from employee stock purchase plan	56,782	—	9	—	9
Stock-based compensation	—	—	619	—	619
Net loss	—	—	—	(14,155)	(14,155)
Balances, December 31, 2009	94,738,400	947	149,012	(182,992)	(33,033)
Issuance of common stock from exercise of stock options	84,193	1	20	—	21
Stock-based compensation	—	—	385	—	385
Net loss	—	—	—	(9,593)	(9,593)
Balances, December 31, 2010	94,822,593	$948	$149,417	$(192,585)	$(42,220)

See accompanying notes consolidated financial statements.

INSITE VISION INCORPORATED

CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended December 31,		
	2010	**2009**	**2008**
OPERATING ACTIVITIES:			
Net loss	$ (9,593)	$(14,155)	$(21,310)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	212	584	413
Impairment of assets	—	615	—
Loss (gain) on sale of assets	—	1	(8)
Amortization of debt issuance costs	418	419	361
Stock-based compensation	385	619	1,030
Changes in operating assets and liabilities:			
Accounts receivable, net	(215)	(1,682)	(736)
Prepaid expenses and other current assets	142	55	598
Accounts payable	46	(876)	(1,034)
Accrued liabilities	151	(369)	(124)
Accrued compensation and related expense	(348)	330	(341)
Accrued royalties	245	321	269
Accrued interest	438	1,738	1,200
Deferred revenues	—	(298)	(9,772)
Net cash used in operating activities	(8,119)	(12,698)	(29,454)
INVESTING ACTIVITIES:			
Purchase of property and equipment	(150)	(34)	(554)
Proceeds from sale of asset	—	4	8
Increase (decrease) in restricted cash and short-term investments	12,500	(17,499)	75
Net cash provided by (used in) investing activities	12,350	(17,529)	(471)
FINANCING ACTIVITIES:			
Issuance of common stock from exercise of options, employee purchase plan and warrants, net of issuance costs	21	9	28
Proceeds from issuance of secured notes payable	—	—	60,000
Payments of debt issuance costs	—	—	(4,164)
Payment of capital lease obligation	(5)	(16)	(15)
Net cash provided by (used in) financing activities	16	(7)	55,849
Net increase (decrease) in cash and cash equivalents	4,247	(30,234)	25,924
Cash and cash equivalents at beginning of year	7,222	37,456	11,532
Cash and cash equivalents at end of year	$11,469	$ 7,222	$ 37,456
Supplemental disclosure of cash flow information:			
Interest received	$ 21	$ 65	$ 603
Interest paid	$ 9,411	$ 7,937	$ 7,045
Income taxes	$ 1	$ 2	$ 5

See accompanying notes to consolidated financial statements.

InSite Vision Incorporated

Notes to Consolidated Financial Statements
For the years ended December 31, 2010, 2009 and 2008

1. Business and Summary of Significant Accounting Policies

InSite Vision Incorporated ("InSite" or the "Company") is an ophthalmic product development company advancing ophthalmic pharmaceutical products to address unmet eye care needs. Our current portfolio of products is based on our proprietary DuraSite® drug delivery technology.

Our DuraSite sustained drug delivery technology is a proven synthetic polymer-based formulation designed to extend the residence time of a drug relative to conventional topical therapies. It enables topical delivery of a drug as a solution, gel or suspension and can be customized for delivering a wide variety of drug candidates. We have focused our research and development and commercial support efforts on the following topical products formulated with our DuraSite drug delivery technology. We may also utilize our DuraSite technology platform for the formulation of new ocular product candidates using either non-proprietary drugs or compounds originally developed by others for non-ophthalmic indications.

Principles of Consolidation. The consolidated financial statements include the accounts of InSite Vision Incorporated as well as its wholly-owned subsidiaries. All intercompany transactions have been eliminated in consolidation.

Industry Segment and Geographic Information. The Company operates in one segment and is focused on developing drugs and drug delivery systems principally for ophthalmic indications. The Company has limited foreign-based operations for the years ended December 31, 2010, 2009 and 2008. All long-lived assets are located in the United States.

Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires the Company to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassifications. Certain amounts in prior years' financial statements have been reclassified to conform to the current presentation. These reclassifications had no impact on previously reported results of operations or stockholders' equity (deficit).

Cash and cash equivalents. The Company considers all highly liquid investments with maturities of 90 days or less from the date of purchase to be cash equivalents.

Short-term investments. The Company considers all investments with original maturities of 12 months or less from the date of purchase to be short-term investments. They are classified as trading securities principally bought and held for the purpose of selling them in the near term, with unrealized gains and losses included in earnings.

Property and Equipment. Property and equipment is stated at cost, less accumulated depreciation and amortization. Depreciation of property and equipment is provided over the estimated useful lives of the respective assets, which range from three to five years, using the straight-line method. Leasehold improvements and property acquired under capital lease are amortized over the lives of the related leases or their estimated useful lives, whichever is shorter, using the straight-line method. Depreciation and amortization expense for the years ended December 31, 2010, 2009 and 2008 were $212,000, $584,000 and $413,000, respectively. The costs of repairs and maintenance are expensed as incurred.

Impairment of Long-Lived Assets. The Company periodically assesses the recoverability of its long-lived assets for which an indicator of impairment exists by determining whether the carrying value of such assets can

be recovered through undiscounted future operating cash flows. If the Company concludes that the carrying value will not be recovered, the Company measures the amount of such impairment by comparing the fair value to the carrying value. The Company recorded an impairment charge of $615,000 in 2009 associated with our corporate restructuring announced in March 2009. The Company impaired laboratory and other equipment, leasehold improvements, and furniture and fixtures located at our corporate headquarters.

Patents. As a result of the Company's research and development efforts, the Company has obtained, or is applying for, a number of patents to protect proprietary technology and inventions. All costs associated with patents for product candidates under development are expensed as incurred. To date, the Company has no capitalized patent costs.

Debt Issuance Costs. Debt issuance costs paid to third parties are capitalized and amortized over the life of the underlying debt, using the straight-line method. Amortization of debt issuance costs for the years ended December 31, 2010, 2009 and 2008 were $418,000, $419,000 and $361,000, respectively, and are included in interest expense and other, net in the Consolidated Statements of Operations. See Note 6, "Secured Notes Payable" for further discussion of the underlying debt.

Fair Value Measurements. The Company measures assets and liabilities at fair value. The levels of fair value measurements are:

Level 1 Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. The Company had no Level 2 assets at December 31, 2010.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. The Company had no material Level 3 assets or liabilities at December 31, 2010.

As of December 31, 2010 and 2009, $16.3 million and $24.3 million, respectively, of our cash, cash equivalents and short-term investments consisted of Level 1 Treasury backed money market funds.

The Company's financial instruments consist mainly of cash equivalents, short-term investments, short-term accounts receivable, accounts payable and debt obligations. Short-term accounts receivable and accounts payable are reflected in the accompanying condensed consolidated financial statements at cost, which approximates fair value due to the short-term nature of these instruments. While the Company believes its valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The Company has long-term debt with fixed interest rates. The Company had $60 million in Level 2 borrowings outstanding as of December 31, 2010, with an interest rate of 16%. As of December 31, 2010, the face value of our long-term debt was estimated to be approximately the fair value based on current market rates.

Revenue Recognition. The Company's revenues are primarily related to royalties on product sales and licensing agreements, and such agreements may provide for various types of payments, including upfront payments, research funding and related fees during the term of the agreement, milestone payments based on the achievement of established development objectives, and licensing fees.

The Company recognizes revenue when four basic criteria are met: persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; the fee is fixed or determinable; and collectability is

reasonably assured. The Company has arrangements with multiple elements. The Company analyzes its multiple element arrangements to determine whether the elements can be separated and accounted for individually as separate units of accounting. An item can generally be considered a separate unit of accounting if all of the following criteria are met: the delivered item(s) has value to the customer on a stand-alone basis; there is objective and reliable evidence of the fair value of the undelivered items(s); and if the arrangement includes a general right of return and delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Company. Items that cannot be divided into separate units are combined with other units of accounting, as appropriate. Consideration received is allocated among the separate units based on their respective fair values or based on the residual value method and is recognized in full when the criteria are met. The Company deems service to be rendered if no continuing obligation exists on the part of the Company.

The Company receives royalties from licensees based on third-party sales. The royalties are recorded as earned in accordance with the contract terms when third-party results are reliably measured and collectability is reasonably assured.

Revenue associated with non-refundable up-front license fees under arrangements where the license fees cannot be accounted for as separate units of accounting is deferred and recognized as revenue on a straight-line basis over the expected term of the Company's continued involvement. Revenues from the achievement of milestones, if deemed substantive, are recognized as revenue when the milestones are achieved, and the milestone payments are due and collectible. If not deemed substantive, the Company would recognize such milestone as revenue on a straight-line basis over the remaining expected term of continued involvement.

Milestones are considered substantive if all of the following conditions are met: the milestone is nonrefundable; achievement of the milestone was not reasonably assured at the inception of the arrangement; substantive effort is involved to achieve the milestone; and the amount of the milestone appears reasonable in relation to the effort expended, the other milestones in the arrangement and the related risk associated with the achievement of the milestone and any ongoing services are priced at fair value.

Research and Development Expenses. Research and development expenses include salaries, benefits, facility costs, services provided by outside consultants and contractors, administrative costs and materials for the Company's research and development activities. The Company recognizes such costs as they are incurred.

The Company accrues and expenses the costs for clinical trial activities performed by third parties based upon estimates of the percentage of work completed over the life of the individual study in accordance with agreements established with contract research organizations and clinical trial sites. The Company determines the estimates through discussions with internal clinical personnel and external service providers as to progress or stage of completion of trials or services and the agreed upon fee to be paid for such services. Costs of setting up clinical trial sites for participation in the trials are expensed immediately as research and development expenses. Clinical trial site costs related to patient enrollment are accrued as patients are entered into the trial.

General and Administrative (G&A) Expenses. G&A expenses include salaries, benefits, facility costs, services provided by outside consultants and contractors, advertising and marketing, investor relations, financial reporting, materials and other expenses related to general corporate and sales and marketing activities. The Company recognizes such costs as they are incurred.

Cost of Revenues. The Company recognizes royalties to third parties and the cost of inventory shipped related to the sale of the Company's products when they are incurred.

Stock-Based Compensation. The Company's stock-based compensation programs consist of stock options granted to employees as well as our employee stock purchase plan (ESPP), based on the grant date fair value of those awards.

The grant date fair value of the award is recognized as expense over the requisite service period. The Company uses the Black-Sholes model to compute the estimated fair value of stock option awards. Using this

model, fair value is calculated based on assumptions with respect to: expected volatility of our common stock price: the periods of time over which employees and members of our board are expected to hold their options prior to exercise; expected dividend yield on our common stock; and risk-free interest rates. Stock-based compensation expense also includes an estimate, which is made at the time of grant, of the number of awards that are expected to be forfeited. The estimate is revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

See Note 10, "Employee Stock-Based Compensation" for further discussion of employee stock-based compensation.

Accounting for Stock Options and Warrants Exchanged for Services. The Company occasionally issues stock options and warrants to consultants of the Company in exchange for services. The Company has valued these options and warrants using the Black-Scholes option pricing model, at each reporting period and has recorded charges to operations over the vesting periods of the individual stock options or warrants. Such charges amounted to approximately $3,000 and $12,000 during the years ended 2009 and 2008, respectively. No charges were incurred in 2010.

Net Loss per Share. Basic net loss per share has been computed using the weighted-average number of common shares outstanding during the period. Dilutive net loss per share is computed using the sum of the weighted-average number of common shares outstanding and the potential number of dilutive common shares outstanding during the period. Potential common shares consist of the shares issuable upon exercise of stock options and warrants. Potentially dilutive securities have been excluded from the computation of diluted net loss per share in 2010, 2009 and 2008 as their inclusion would be anti-dilutive.

The following table sets forth the computation of basic and diluted net income (loss) per share:

	Year Ended December 31,		
(in thousands, except per share data)	2010	2009	2008
Numerator:			
Net loss	$ (9,593)	$(14,155)	$(21,310)
Denominator:			
Weighted-average shares outstanding	94,774	94,710	94,607
Effect of dilutive securities:			
Stock options and warrants	—	—	—
Weighted-average shares outstanding for diluted loss	94,774	94,710	94,607
Net loss per share:			
Basic	$ (0.10)	$ (0.15)	$ (0.23)
Diluted	$ (0.10)	$ (0.15)	$ (0.23)

For the years ended December 31, 2010, 2009 and 2008, due to the loss applicable to common stockholders, loss per share is based on the weighted average number of common shares only, as the effect of including equivalent shares from stock options and warrants would be anti-dilutive. At December 31, 2010, 2009 and 2008, 10,293,478, 13,908,611 and 21,471,962 options and warrants were excluded from the calculation of diluted earnings per share because the effect was anti-dilutive.

Accounting for Materials Purchased for Research and Development. The Company expenses materials for research and development activities when the obligation for the items is incurred.

Key Suppliers. The Company is dependent on single or limited source suppliers for certain materials used in its research and development and commercial activities. The Company has generally been able to obtain

adequate supplies of these components. However, an extended interruption in the supply of these components currently obtained from single or limited source suppliers could adversely affect the Company's research and development and commercial efforts.

Income Taxes. Income tax expense has been provided using the liability method. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates that will be in effect when these differences reverse. The Company provides a valuation allowance against net deferred tax assets if, based upon the available evidence, it is not more likely than not that the deferred tax assets will be realized.

The financial statement recognition of the benefit for a tax position is dependent upon the benefit being more-likely-than not to be sustainable upon audit by the applicable taxing authority. If this threshold is met, the tax benefit is then measured and recognized at the largest amount that is greater than 50 percent likely of being realized upon ultimate settlement. For years ended December 31, 2010, 2009 and 2008, the Company has not recognized any income tax positions that were deemed uncertain under the recognition thresholds and measure attributes prescribed by authoritative guidance.

The Company's policy is to recognize interest and penalties related to the underpayment of income taxes as a component of income tax expense. To date, there have been no interest or penalties charged to the Company in relation to the underpayment of income taxes.

Significant Customers and Risk. All revenues recognized and/or deferred were from AzaSite licensees. The Company is entitled to receive royalty revenue from net sales of AzaSite under the terms of its agreements with Inspire and other licenses, and accordingly, all trade receivables are concentrated with these parties. Due to the nature of these agreements, these parties have significant influence over the commercial success of AzaSite. Revenues from Inspire represented approximately 92%, 85% and 100% of total revenues for the years ended December 31, 2010, 2009 and 2008, respectively.

Credit Risk. Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, cash equivalents and short-term investments. The Company's cash, cash equivalents and short-term investments are primarily deposited in demand accounts with one financial institution.

Risks from Third Party Manufacturing Concentration. The Company relies on a single source manufacturer for each of its product candidates and on a single source manufacturer for the active pharmaceutical ingredient in its product candidates. Inspire is responsible for the manufacturing of AzaSite in North America and relies on a single source manufacturer for the product and on a single source manufacturer for the active pharmaceutical ingredient in the product. Accordingly, delays in the manufacture of the product or product candidates could adversely impact the marketing of the Company's product or the development of the Company's product candidates. Furthermore, the Company has no control over the manufacture and the overall product supply chain of products for which it is entitled to receive revenue.

Recent Accounting Pronouncements.

In October 2009, the FASB issued an amendment to accounting standards related to multiple-deliverable revenue arrangements. The amendment requires entities to allocate revenue in multiple-deliverable revenue arrangements using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The amendments eliminate the residual method of revenue allocation and require revenue to be allocated using the relative selling price method. The standard is effective on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning after June 15, 2010. The Company is currently evaluating the impact to the Company's financial position and results of operations.

In January 2010, the FASB issued an amendment to accounting standards related to fair value disclosures. The amendment requires entities to provide enhanced disclosures about transfers into and out of the Level 1 (fair

value determined based on quoted prices in active markets for identical assets and liabilities) and Level 2 (fair value determined based on significant other observable inputs) classifications, provide separate disclosure about purchases, sales, issuances and settlements relating to the tabular reconciliation of beginning and ending balances of the Level 3 (fair value determined based on significant unobservable inputs) classification and provide greater disaggregation for each class of assets and liabilities that use fair value measurements. The standard is effective for interim and annual reporting periods beginning after December 31, 2009, except for the Level 3 disclosure. The Company adopted this standard during the period ended March 31, 2010. The adoption did not impact the Company's consolidated financial position or results of operations. The Level 3 disclosure is effective for interim and annual reporting periods beginning after December 31, 2010. The Company expects that the adoption of the Level 3 disclosure will not materially impact the Company's consolidated financial position or results of operations, other than additional disclosure requirements.

2. License Agreements

In December 2003, we completed the sale of our drug candidate for the treatment of ocular infections to Bausch & Lomb Incorporated ("Bausch & Lomb"), pursuant to a Purchase Agreement and a License Agreement. The drug candidate, Besivance, was developed by Bausch & Lomb. In May 2009, the FDA approved Besivance to treat bacterial conjunctivitis (pink eye). Besivance was launched in the United States by Bausch & Lomb and Pfizer, Inc. in the last half of 2009.

On February 15, 2007, the Company entered into a license agreement for AzaSite™ with Inspire under which the Company licensed to Inspire exclusive development and commercialization rights in the United States and Canada, for topical anti-infective products containing azithromycin as the sole active ingredient for human ocular or ophthalmic indications. The Company also granted Inspire an exclusive sublicense under the Pfizer patent rights the Company has licensed under the Pfizer License discussed below. Inspire has the right to grant sublicenses under the terms of the Inspire License.

Inspire paid the Company an upfront license fee of $13 million on February 15, 2007 and on May 11, 2007 paid an additional $19 million upon regulatory approval by the U.S. FDA. Inspire also pays the Company a royalty on net sales of AzaSite in the United States and Canada. The royalty rate is 20% of net sales in the first two years of commercialization and 25% thereafter. Inspire is obligated to pay the Company royalties under the Inspire License for the longer of (i) eleven years from the launch of the first product, and (ii) the period during which a valid claim under a patent exists. For five years after the first year of commercial sale, Inspire will pay the Company certain tiered minimum royalties. The royalties discussed above are subject to certain reductions in the event of patent invalidity, generic competition, uncured material breach or in the event that Inspire is required to pay license fees to third parties for the continued use of AzaSite.

The Company also entered into a supply agreement, or the Supply Agreement, with Inspire on February 15, 2007 for the active pharmaceutical ingredient azithromycin. The Company had previously entered into a third-party supply agreement for the production of such active ingredient.

The Company recognized the upfront license fee and milestone payment totaling $32 million ratably over the period that the Company was required to continue to provide services under the license agreement, which ended in April 2008, under the contingency-adjusted performance model of revenue recognition. During the years ended December 31, 2008 and December 31, 2007, the Company recognized $9.9 million and $22.1 million, respectively, of the license fee and milestone payment as revenue.

In August 2007, Inspire commercially launched AzaSite in the United States. Correspondingly, during the years ended December 31, 2010, 2009, and 2008, the Company recognized $10,652,000, $8,000,000 and $3,596,000, respectively, of royalties related to sales of AzaSite by Inspire. Additionally, during the years ended December 31, 2010 and 2009, the Company recognized $258,000 and $325,000, respectively, of revenue from Inspire for the sales of the active ingredient, azithromycin, under the Supply Agreement, sales of AzaSite inventory and for contract services provided.

On February 15, 2007, the Company entered into a worldwide, exclusive, royalty-bearing license agreement with Pfizer Inc. under Pfizer's patent family titled "Method of Treating Eye Infections with Azithromycin" for ocular anti-infective product candidates known as AzaSite and AzaSite Plus (the "Pfizer License"). Under the Pfizer License, the Company is required to pay Pfizer a low single digit royalty based on net sales of the licensed products and to use reasonable commercial efforts to seek regulatory approval for and market licensed products. The Pfizer License provides the Company the right to grant sublicenses thereunder, subject to Pfizer's prior approval, which approval shall not be unreasonably withheld. Pfizer approved the sublicense granted to Inspire. Based on the royalty report provided by Inspire, for the years ended December 31, 2010, 2009 and 2008, the Company recorded third-party royalties of $1,491,000, $1,224,000 and $630,000, respectively, due primarily under the Pfizer License.

We have entered into, and will continue to pursue additional licensing agreements, corporate collaborations and service contracts. In our international licensing agreements, the licensee is responsible for obtaining regulatory approval and will generally pay us a double digit royalty on net sales of AzaSite in these countries, if approved by regulatory authorities. We will be responsible for providing AzaSite inventory to these licensees at a fee set forth in each respective license agreement. There can be no assurance that we will be able to negotiate acceptable collaborative, licensing or service agreements, or that our existing arrangements will be successful or renewed or that it will not be terminated.

3. Short-term Investments

As of December 31, 2010 and 2009, the Company had $5.0 million and $17.5 million in short-term investments, respectively. The Company's investment policy is to limit the risk of principal loss and to ensure safety of invested funds by generally attempting to limit market risk. Accordingly, the Company's short-term investments were invested in United States Treasury securities with original maturities of twelve months or less. They are classified as trading securities principally bought and held for the purpose of selling them in the near term, with unrealized gains and losses included in earnings. At December 31, 2010 and 2009, the Company had less than $1,000 of unrealized gains included in earnings.

4. Accounts Receivable, net

Accounts receivable, net represent amounts due to the Company from its licensees, Inspire and other third parties. As of December 31, 2010, the Company recorded a $50,000 bad debt allowance related to these accounts receivable. At December 31, 2009, the Company did not record a bad debt allowance related to any accounts receivable as all amounts were reasonably expected to be collected. The need for a bad debt allowance is evaluated each reporting period based on our assessment of the collectability of the amounts.

5. Property and Equipment, net

Property and equipment, net consisted of the following (in thousands):

	December 31,	
	2010	**2009**
Laboratory and other equipment	$1,094	$ 955
Leasehold improvements	39	29
Furniture and fixtures	14	33
	1,147	1,017
Accumulated depreciation and amortization	(900)	(708)
Property and equipment, net	$ 247	$ 309

6. Secured Notes Payable

In February 2008, the Company's wholly-owned subsidiary, Azithromycin Royalty Sub, LLC completed a private placement of $60.0 million in aggregate principal amount of non-convertible, non-recourse promissory notes due in 2019. Net proceeds from the financing were approximately $55.3 million after transaction costs of approximately $4.7 million. In addition, $5.0 million of the proceeds was set aside for interest reserves. The annual interest rate on the notes is 16% with interest payable quarterly in arrears beginning May 15, 2008. The notes are secured by, and will be repaid from, royalties to be paid to the Company by Inspire Pharmaceuticals from sales of AzaSite in the United States and Canada. The secured notes payable are non-recourse to InSite Vision Incorporated. When the AzaSite royalties received for any quarter exceed the interest payments and certain expenses due that quarter, the excess will be applied to the repayment of principal of the notes until the notes have been paid in full. Any shortfall of interest payments from the royalty payments will be paid out of the interest reserves. As of December 31, 2010, no balance remained in the interest reserve. Further shortfalls, if any, can be paid by the Company at its option to avoid default under the agreement. The notes may be redeemed at the Company's option, subject to the payment of a redemption premium through May 2012. As of December 31, 2010, the $60.0 million of secured notes payable was classified as long-term.

At December 31, 2010, the estimated future principal payments on the notes, based on minimum royalty income covered by the agreement and future projected sales, were as follows (in thousands):

Year Ending December 31,	
2011	$ 1,503
2012	6,057
2013	8,978
2014	3,368
2015	4,216
Thereafter	35,878
Total secured notes payable	$60,000

7. Commitments and Contingencies

The Company has entered into certain license agreements that require us to make royalty payments for the life of the licensed patents. The estimated royalties due under these agreements is approximately $13.7 million for the periods 2011 through 2019. This contractual obligation is reflected in the Company's financial statements once the related obligation becomes due.

Capital lease obligations represent the present value of future rental payments under capital lease agreements for telephones and telephone equipment. At December 31, 2010 and 2009, the Company had $13,000 of capital leased equipment with accumulated depreciation of $13,000 and $12,000, respectively. The Company has $5,000 of future minimum payments under capital leases for 2011 and no future payments in 2012 and thereafter.

The Company conducts its operations from leased facilities in Alameda, California under non-cancelable operating lease agreements that expire in 2013. Lease payments include rent and the Company's pro-rata share of operation expenses. The Company subleases a portion of the facility under a lease agreement that expires in 2013. Lease income includes rent and a pro-rata share of operation expenses. For accounting purposes, the Company is amortizing all rent payments and receipts ratably over the life of the lease. Rent expense for the years ended December 31, 2010, 2009 and 2008, was $757,000, $776,000, and $776,000, respectively. Future minimum lease payments under the operating lease and future cash receipts from the sublease, were as follows (in thousands):

Year Ending December 31,	Operating Lease Cash Payments	Operating Sublease Cash Receipts	Operating Lease Cash Payments, net
2011	$ 798	$ 54	$ 744
2012	822	98	724
2013	848	106	742
2014	—	—	—
2015 and thereafter	—	—	—
Total	$2,468	$258	$2,210

8. Income Taxes

The provision of income taxes is determined using an estimated annual effective tax rate, which is generally less than the U.S. federal statutory rates, primarily because of research and development credits (R&D credits) and deductions available in the United States for domestic production activities. The Company's effective tax rate may be subject to fluctuations during the year as new information is obtained, which may affect the assumptions management uses to estimate the annual effective tax rate, including factors such as valuation allowances against deferred tax assets, the recognition and de-recognition of tax benefits related to uncertain tax positions, expected utilization of R&D credits and changes in temporary differences between financial reporting basis and tax basis of our assets and liabilities along with net operating losses and tax credit carryovers. The effective income tax rate was 0.0% for the year ended December 31, 2010 due to the use of previously generated net operating losses. There was no provision for income taxes for the years ended December 31, 2009 and 2008 due to the Company's net operating losses.

The Company's effective tax rate differs from the U.S. federal statutory income tax rate for the years ended December 31, 2010, 2009 and 2008, principally due to the following:

	2010	2009	2008
Tax provision at federal statutory rate	34.0%	34.0%	34.0%
State taxes, net of federal benefit	4.0%	6.0%	6.0%
Other permanent differences	1.5%	1.8%	3.8%
Credits	-1.9%	-3.4%	-3.6%
Valuation allowance	-37.6%	-38.4%	-40.2%
Effective tax rate	0.0%	0.0%	0.0%

Significant components of the Company's deferred tax assets for federal and state income taxes as of December 31, 2010 and 2009 are as follows (in thousands):

	2010	2009
Deferred tax assets:		
Net operating loss carryforwards	$ 38,761	$ 38,951
Tax credit carryforwards	7,115	6,931
Capitalized research and development	13,743	14,329
Depreciation	689	621
Other	149	197
Total deferred tax assets	60,457	61,029
Valuation allowance	(60,457)	(61,029)
Net deferred tax assets	$ —	$ —

During the year ended December 31, 2010, the valuation allowance decreased by $0.6 million primarily due to the expirations of net operating losses. During the year ended December 31, 2009, the valuation allowance increased by $1.2 million primarily due to the increase in net operating losses.

At December 31, 2010, the Company had net operating loss carryforwards for federal income tax purposes of approximately $95.6 million, which expire in the years 2011 through 2030 and federal tax credits of approximately $3.0 million, which expire in the years 2010 through 2028. At December 31, 2010, the Company also has net operating loss carryforwards for state income tax purposes of approximately $104.3 million which expire in the years 2011 through 2030 and state research and development tax credits of approximately $4.0 million which carryforward indefinitely.

Utilization of the Company's federal and state net operating loss carryforwards and research and development tax credits are subject to an annual limitation against taxable income in future periods due to the ownership change limitations provided by the Internal Revenue Code. As a result of this annual limitation, a significant portion of these carryforwards will expire before ultimately becoming available for offset against taxable income. Additional losses and credits will be subject to limitation if the Company incurs another change in ownership in the future.

The Company files income tax returns in the U.S. federal and California jurisdictions. The Company is no longer subject to tax examinations for years before 2007 for federal returns and 2006 for California returns, except to the extent that it utilizes net operating losses or tax credit carryforwards that originated before those years. The Company is not currently under audit by any major tax jurisdiction nor has it been in the past.

9. Stockholders' Equity (Deficit)

In 2010, the Company received approximately $21,000 from the exercise of options to purchase 84,193 shares of common stock issued to employees.

In 2009, the Company received approximately $9,000 from the issuance of 56,782 shares acquired under the employee stock purchase plan.

In 2008, the Company received approximately $28,000 from the issuance of 96,169 shares acquired under the employee stock purchase plan.

The following table shows the detail of outstanding warrants as of December 31, 2010. All of the outstanding warrants have cashless exercise provisions.

Date Issued	Warrant Shares	Exercise Price	Expiration Date	Cash if Exercised
January 11, 2006	400,000	0.82	January 10, 2011	$ 328,000
August 16, 2006	958,015	1.51	August 15, 2011	1,446,603
Total	1,358,015			$1,774,603
Weighted-average exercise price per share				$ 1.31

10. Stock-based Compensation

Equity Incentive Program

Prior to October 15, 2007, the Company granted options under a stock option plan adopted in 1994 and amended thereafter (the "1994 Plan"), that allowed for the granting of non-qualified stock options, incentive stock options and stock purchase rights to the Company's employees, directors, and consultants. On October 15, 2007, the Company's stockholders approved a new equity incentive plan, the 2007 Performance Incentive Plan (the "2007 Plan"), that provides for grants of options and other equity-based awards to the Company's employees, directors and consultants. The Company's authority to grant new awards under the 1994 Plan terminated upon stockholder approval of the 2007 Plan. Options granted under these plans expire 10 years after the date of grant and become exercisable at such times and under such conditions as determined by the Company's Board of Directors or a committee appointed by the Board (generally with 25% vesting after one year and the balance vesting on a daily basis over the next three years of service). Upon termination of the optionee's service, unvested options terminate, and vested options generally expire at the end of three months. Only nonqualified stock options have been granted under these plans to date. On January 1 of each calendar year during the term of the 2007 Plan, the shares of Common Stock available for issuance will be increased by the lesser of 2% of the total outstanding shares of Common Stock on December 31 of the preceding calendar year, or 3,000,000 shares.

Employee Stock Purchase Plans

The Company maintained an employee stock purchase plan, adopted in 1994 and amended thereafter (the "Purchase Plan"), until August 2009. In August 2009, the Purchase Plan was suspended. No new offering period will commence and no additional shares will be added to the Purchase Plan under its evergreen provision unless and until approved by the Company's Board of Directors. The Purchase Plan operated in 24-month "offering periods" that are each divided into four six-month "purchase periods." The Purchase Plan allowed eligible employees to purchase Common Stock at 85% of the lower of the fair market value of the Common Stock on the first day of the applicable offering period or the fair market value of the Common Stock on the last day of the applicable purchase period. Purchases were limited to 10% of each employee's eligible compensation, subject to certain Internal Revenue Service restrictions. All of the Company's employees were eligible to participate in the Purchase Plan after certain service periods were met. The number of shares available for issuance under the Purchase Plan was automatically increased on the first trading day in January each calendar year, by an amount equal to 0.5% of the total number of shares of Common Stock outstanding on the last trading day in December in the immediately preceding calendar year, but in no event will any such annual increase exceed 125,000 shares. During the year ended December 31, 2009, 56,782 shares were issued under the Purchase Plan. As of December 31, 2010, 515,183 shares were reserved for issuance under the Purchase Plan. As of December 31, 2010, there was no remaining unrecorded deferred stock-based compensation expense related to the Purchase Plan.

Stock-based Compensation

Stock-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as expense over the requisite service period. All of the Company's stock compensation is accounted for as an equity instrument.

The effect of recording stock-based compensation for the year ended December 31, 2010, 2009 and 2008 was as follows (in thousands):

	Year Ended December 31,		
	2010	2009	2008
Stock-based compensation expense by type of award:			
Employee stock options	$385	$588	$ 950
Employee stock purchase plan	—	28	68
Non-employee stock options	—	3	12
Total stock-based compensation	$385	$619	$1,030

During the years ended December 31, 2010 and 2009, respectively, the Company granted options to purchase 5,424,374 and 3,185,000 shares of common stock with an estimated total grant date fair value of $1.4 million and $0.5 million. Based on the Company's historical experience of option pre-vesting cancellations and estimates of future forfeiture rates, the Company has assumed an annualized forfeiture rate of 10% for its options for all periods disclosed. Accordingly, for the years ended December 31, 2010 and 2009, the Company estimated that the stock-based compensation for the awards not expected to vest were $0.3 million and $0.1 million, respectively.

As of December 31, 2010 and 2009, unrecorded deferred stock-based compensation balance related to stock options were $1.2 million and $0.5 million, respectively, and will be recognized over an estimate weighted-average amortization period of 3.1 years and 2.2 years, respectively.

Fair Value Assumptions

The fair value of each option grant is estimated using the Black-Scholes valuation model on the date of grant and the graded-vesting method with the following weighted-average assumptions:

	Year ended December 31,		
Stock Options	2010	2009	2008
Risk-free interest rate	1.3% - 2.6%	1.7% - 2.4%	2.6% - 3.3%
Expected term (years)	5	5	5
Expected dividends	0.0%	0.0%	0.0%
Volatility	87.8%	82.1%	76.6%

	Year ended December 31,	
Employee Stock Purchase Plan	2009	2008
Risk-free interest rate	1.7%	3.0%
Expected term (years)	1.5	1.5
Expected dividends	0.0%	0.0%
Volatility	80.5%	73.8%

The dividend yield of zero is based on the fact that the Company has never paid cash dividends and has no present intention to pay cash dividends. Expected volatility is based on the combination of historical volatility of the Company's common stock and the common stock of the Company's competitors, the expected moderation in future volatility over the period commensurate with the expected life of the options and other factors. The risk-free interest rates are taken from the Daily Federal Yield Curve Rates as of the grant dates as published by the Federal Reserve and represent the yields on actively traded Treasury securities for terms equal to the expected term of the options. The expected term calculation is based on the terms utilized by the Company's competitors, observed historical option exercise behavior and post-vesting forfeitures of options by the Company's employees.

The following is a summary of activity under the Company's stock option plans for the indicated periods:

	Number of shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2007	7,003,855	$1.09	6.84	$349
Granted	630,250	0.47		
Exercised	—	0.00		
Forfeited	(343,518)	1.09		
Expired	(1,076,561)	1.22		
Outstanding at December 31, 2008	6,214,026	1.00	3.67	0
Granted	3,185,000	0.26		
Exercised	—	0.00		
Forfeited	(591,460)	0.25		
Expired	(1,401,281)	1.03		
Outstanding at December 31, 2009	7,406,285	0.74	4.93	296
Granted	5,424,374	0.37		
Exercised	(84,193)	0.24		
Forfeited	(325,804)	0.34		
Expired	(3,485,199)	1.08		
Outstanding at December 31, 2010	8,935,463	$0.40	8.79	$211
Options vested and expected to vest at December 31, 2010	8,070,354	$0.41	8.70	$203
Options exercisable at December 31, 2010	2,889,719	$0.52	7.28	$ 93

At December 31, 2010, the Company had 1,870,982 shares of common stock available for grant under its 2007 Plan. The weighted average grant date fair value of options granted during the years ended December 31, 2010, 2009 and 2008 were $0.25, $0.17 and $0.26, respectively. The total intrinsic value of options exercised during the year ended December 31, 2010 was $13,000. No options were exercised during the years ended December 31, 2009 and 2008.

The following table summarizes information concerning outstanding and exercisable options as of December 31, 2010:

	Option Outstanding			Options Vested and Exercisable	
		Weighted-Average			
Range of Exercise Prices	Number Outstanding	Contractual Life	Exercise Price	Number Exercisable	Weighted-Average Exercise Price
$0.20 - $0.20	1,050,000	8.13	$0.20	490,270	$0.20
$0.22 - $0.28	480,000	8.29	0.23	201,952	0.22
$0.33 - $0.33	900,000	9.97	0.33	—	0.00
$0.35 - $0.35	2,844,374	9.92	0.35	—	0.00
$0.36 - $0.36	300,000	7.82	0.36	300,000	0.36
$0.38 - $0.38	900,000	8.96	0.38	900,000	0.38
$0.41 - $0.41	25,000	2.95	0.41	25,000	0.41
$0.42 - $0.42	1,430,000	9.25	0.42	—	0.00
$0.52 - $1.50	906,089	5.13	0.85	872,497	0.85
$1.59 - $2.20	100,000	5.10	1.71	100,000	1.71
	8,935,463	8.79	$0.40	2,889,719	$0.52

At December 31, 2009 and 2008 options to purchase 4,610,202 and 5,287,717 shares of common stock were exercisable at weighted-average exercise prices of $1.02 and $1.05, per share, respectively.

The following table details the Company's nonvested stock options activity for the year ended December 31, 2010:

	Number of shares	Weighted-Average Grant-Date Fair Value
Outstanding at December 31, 2009	2,796,083	$0.19
Granted	5,424,374	0.25
Vested	(1,848,906)	0.19
Forfeited	(325,807)	0.23
Outstanding at December 31, 2010	6,045,744	$0.23

The weighted-average grant date fair value of nonvested stock options is calculated using the Black-Scholes valuation model on the date of grant.

11. Restructuring Charge

In December 2008, the Company announced a corporate restructuring plan to focus on the Company's growth opportunities and conserve resources. As of December 31, 2010, the restructuring plan reduced the Company's personnel by 39 employees. When affected employees were notified of their termination, the Company recorded the severance related costs. Severance totaled approximately $2.4 million of which $0.2 million was a non-cash transaction. In 2008, $1.9 million was recorded as severance expense in the Consolidated Statement of Operations. The remaining $0.5 million was recorded as severance expense in the Condensed Consolidated Statement of Operations in 2009. The Company has not incurred severance related costs in 2010.

The following table summarizes the activity for the accrued severance included in accrued compensation and related expense in the Consolidated Balance Sheets (in thousands):

Accrual at December 31, 2009	$ 157
Payments made	(157)
Accrual at December 31, 2010	$ —

The remaining liability of $157,000 was paid in the first quarter of 2010.

In February 2009, the Company announced a plan to develop and implement a new strategy to build shareholder value and further reduce costs. Based on a thorough analysis of the Company's business and the marketplace, the Company believed the best path forward was a strategy that monetized its current assets and either acquired promising new product opportunities or entered into a sales transaction for the Company. Based on that business strategy, during the first quarter of 2009, the Company determined that the carrying value of its laboratory and other equipment, leasehold improvements, and furniture and fixtures would not be recovered through undiscounted future operating cash flows. To determine the fair value of assets, the Company obtained quoted market prices for similar assets. The Company adjusted the carrying amount of the assets to the lower of the carrying value or fair value and recorded $0.6 million as impairment expense in the Condensed Consolidated Statement of Operations in 2009.

12. Legal Proceedings

The Company is subject to various claims and legal actions during the ordinary course of its business. On November 30, 2009, a patent interference was declared before the Board of Patent Appeals and Interferences on

certain U.S. patents covering AzaSite. Regents of the University of California assert that the inventions contained in these patents were made by a former employee of the university alone, and without collaboration with InSite Vision. They are asserting that they own those inventions, and that they are entitled to an award of priority of invention and a judgment that the inventions are not patentable to InSite Vision. InSite Vision believes the University's assertions are without merit and intends to vigorously contest those assertions.

We believe that there are currently no other claims or legal actions that would have a material adverse impact on our financial position, operations or potential performance.

13. Quarterly Results (Unaudited)

The following table is a summary of the quarterly results of operations for the years ended December 31, 2010 and 2009. The Company believes that the following information reflects all normal recurring adjustments necessary for a fair presentation of the information for the periods presented. The operating results for any quarter are not necessarily indicative of results for any future period.

	2010			
(In thousands, except per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	$ 2,282	$ 2,470	$ 3,235	$ 3,880
Cost of revenues	303	336	625	463
Gross profit	1,979	2,134	2,610	3,417
Income (loss) from operations	(384)	111	220	708
Net loss	(2,939)	(2,450)	(2,345)	(1,859)
—basic	$ (0.03)	$ (0.03)	$ (0.02)	$ (0.02)
—diluted	$ (0.03)	$ (0.03)	$ (0.02)	$ (0.02)

	2009			
(In thousands, except per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	$ 2,252	$ 1,874	$ 2,209	$ 3,463
Cost of revenues	216	266	316	751
Gross profit	2,036	1,608	1,893	2,712
Income (loss) from operations	(2,862)	(1,222)	(539)	502
Net loss	(5,357)	(3,698)	(3,052)	(2,048)
—basic	$ (0.06)	$ (0.04)	$ (0.03)	$ (0.02)
—diluted	$ (0.06)	$ (0.04)	$ (0.03)	$ (0.02)

14. Subsequent Events

The Company evaluated subsequent events through the date on which the financial statements were issued, and has determined that there are no subsequent events that require adjustments or disclosure to the financial statements for the year ended December 31, 2010.

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

None

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of the end of the period covered by this report (the "Evaluation Date"). Based upon the evaluation, our principal executive officer and principal financial officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure. Disclosure controls are controls and procedures designed to reasonably ensure that information required to be disclosed in our reports filed under the Exchange Act, such as this report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls include controls and procedures designed to reasonably ensure that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure. Our quarterly evaluation of disclosure controls includes an evaluation of some components of our internal control over financial reporting, and internal control over financial reporting is also separately evaluated on an annual basis for purposes of providing the management report which is set forth below.

Report of Management on Internal Control Over Financial Reporting. Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurances with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2010. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission in Internal Control — Integrated Framework. Based on its assessment using those criteria, our management concluded that, as of December 31, 2010, our internal control over financial reporting was effective.

Changes in Internal Control Over Financial Reporting. There were no changes in our internal control over financial reporting (as defined in Exchange act Rule 13a-15(f)) during the quarter ended December 31, 2010 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

Not applicable.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

(a) Information regarding our executive officers appears under the heading "Executive Officers of the Company" in Item 1 of Part I of this Annual Report on Form 10-K.

(b) The remaining information required by this Item will appear under the headings labeled "Nominees for Directors," "Board Committees and Meetings," "Audit Committee Matters," "Corporate Governance" and "Section 16(a) Beneficial Ownership Reporting Compliance" of our Proxy Statement and such required information is incorporated herein by reference.

Item 11. Executive Compensation

The information required by this Item will appear under the headings labeled "Director Compensation for 2010," "Compensation, Discussion and Analysis," "Compensation of Named Executive Officers," "Summary Compensation Table for 2010," "Grants of Plan Based Awards in 2010," "Outstanding Equity Awards at Fiscal 2010 Year End," " Option Exercises and Stock Vested in 2010," "Non-Qualified Deferred Compensation for 2010," "Compensation Committee Interlocks and Insider Participation" and "Compensation Committee Report" of our Proxy Statement and such required information is incorporated herein by reference.

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

The information required by this Item will appear under the headings labeled "Equity Compensation Plans" and "Beneficial Ownership of Principal Stockholders, Directors and Management" of our Proxy Statement and such required information is incorporated herein by reference.

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

The information required by this Item will appear under the headings labeled "Certain Relationships and Related Persons Transactions" and "Director Independence" of our Proxy Statement and such required information is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services

Audit Fees

The information required by this Item will appear under the headings labeled "Audit Committee Matters" and "Principal Accounting Fees and Services" of our Proxy Statement and such required information is incorporated herein by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a)(1) Financial Statements

The Financial Statements and Report of Independent Auditors are included in Item 8 of Part II of this Annual Report on Form 10-K. See index to consolidated financial statements at Item 8 of Part II of this Annual Report on Form 10-K.

(2) Financial Statement Schedules

The information required under this Item appears in the Financial Statements or notes thereto included in Item 8 of Part II of this Annual Report on Form 10-K. See index to consolidated financial statements at Item 8 of this Annual Report on Form 10-K.

(3) Exhibits

The information required under this Item appears under the heading "Exhibit Index" of this Annual Report on Form 10-K.

SIGNATURES

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

Dated: March 4, 2011

INSITE VISION INCORPORATED

By: /s/ LOUIS DRAPEAU

Louis Drapeau
Chief Financial Officer
(Principal Financial Officer)

POWER OF ATTORNEY

KNOW ALL PEOPLE BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Louis C. Drapeau, his attorney in fact and agent, with the power of substitution and resubstition, for him and in his name, place and stead, in any and all capacities, to sign any amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorney in fact, or his substitutes or agents, each acting alone, may do or cause to be done by virtue thereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Name	Capacity	Date
/s/ TIMOTHY RUANE **Timothy Ruane**	Chief Executive Officer and Director (Principal Executive Officer)	March 4, 2011
/s/ LOUIS DRAPEAU **Louis Drapeau**	Chief Financial Officer (Principal Financial Officer)	March 4, 2011
/s/ RICK D. ANDERSON **Rick D. Anderson**	Director	March 4, 2011
/s/ TIMOTHY P. LYNCH **Timothy P. Lynch**	Director	March 4, 2011
/s/ TIMOTHY MCINERNEY **Timothy McInerney**	Director	March 4, 2011
/s/ EVAN S. MELROSE, M.D. **Evan S. Melrose, M.D.**	Chairman of Board, Director	March 4, 2011
/s/ ROBERT O'HOLLA **Robert O'Holla**	Director	March 4, 2011
/s/ ANTHONY J. YOST **Anthony J. Yost**	Director	March 4, 2011

EXHIBIT INDEX

Number	Exhibit Table
3.1[1]	Restated Certificate of Incorporation as filed with the Delaware Secretary of State on October 25, 1993.
3.2[2]	Certificate of Designations, Preferences and Rights of Series A Convertible Preferred Stock as filed with the Delaware Secretary of State on September 11, 1997.
3.3[2]	Certificate of Correction of the Certificate of Designations, Preferences and Rights of Series A Convertible Preferred Stock as filed with the Delaware Secretary of State on September 26, 1997.
3.4[3]	Certificate of Designations, Preferences and Rights of Series A-1 Preferred Stock as filed with the Delaware Secretary of State on July 3, 2002.
3.5[4]	Certificate of Amendment to Restated Certificate of Incorporation as filed with the Delaware Secretary of State on June 3, 1994.
3.6[5]	Certificate of Amendment to Restated Certificate of Incorporation as filed with the Delaware Secretary of State on July 20, 2000.
3.7[5]	Certificate of Amendment to Restated Certificate of Incorporation as filed with the Delaware Secretary of State on June 1, 2004.
3.8[6]	Certificate of Amendment to Restated Certificate of Incorporation as filed with the Delaware Secretary of State on October 23, 2006
3.9[7]	Amended Bylaws, as amended on June 2, 2008.
4.1	Reference is made to Exhibits 3.1 through 3.9.
10.1[8]	InSite Vision Incorporated Amended and Restated Employee Stock Purchase Plan adopted October 15, 2007.
10.2[9HH]	InSite Vision Incorporated 1994 Stock Option Plan (Amended and Restated as of June 8, 1998).
10.3[8HH]	InSite Vision Incorporated 2007 Performance Incentive Plan.
10.4[8]	Form of Nonqualified Stock Option Agreement (2007).
10.5[8]	Form of Incentive Stock Option Agreement (2007).
10.6[10]	Form of Indemnification Agreement between the Company and its directors and officers.
10.7[11]	Form of Employee's Proprietary Information and Inventions Agreement.
10.8[12H]	License Agreement dated as of October 9, 1991 by and between the Company and CIBA Vision Corporation, as amended October 9, 1991.
10.9[13]	Facilities Lease, dated September 1, 1996, between the Registrant and Alameda Real Estate Investments.
10.10[14H]	Timolol Development Agreement dated July 18, 1996 by and between the Company and Bausch & Lomb Pharmaceuticals, Inc.
10.11[2H]	License Agreement, dated July 1, 1997, by and between the University of Connecticut Health Center and the Company.
10.12[2H]	License Agreement, dated August 19, 1997, by and between the University of Rochester and the Company.
10.13[15]	Amendment No. 1 to Marina Village Office Tech Lease, dated July 20, 2001 and effective January 1, 2002.

Number	Exhibit Table
10.14[16H]	License Agreement, dated December 21, 2001 by and between the Company and The University of Connecticut Health Center.
10.15[17H]	ISV-403 Asset Purchase Agreement, dated December 19, 2003, between the Company and Bausch & Lomb, Inc.
10.16[18]	Form of Class A Warrants issued under Subscription Agreement dated March 26, 2004.
10.17[18]	Form of Class B Warrants issued under Subscription Agreement dated March 26, 2004.
10.18[18]	Form of Placement Warrant issued pursuant to Placement Agreement dated February 12, 2004.
10.19[4]	Form of Common Stock Warrant issued under Subscription Agreement dated May 26, 2005.
10.20[4]	Form of Placement Agent Warrant, dated as of May 9, 2005.
10.21[19]	Warrant, dated as of October 10, 2005, for the purchase of 922,800 shares of Common Stock of the Company.
10.22[20]	Form of Warrant, dated as of January 11, 2006.
10.23[20]	Form of Placement Agent Warrant, dated as of January 11, 2006.
10.24[21]	Form of Warrant, dated as of August 15, 2006.
10.25[5]	Amendment No. 3 to Marina Village Office Tech Lease, dated November 28, 2006.
10.26[22H]	Exclusive License Agreement, dated as of February 15, 2007, by and between the Company and Pfizer, Inc. and Pfizer Products, Inc.
10.27[22H]	License Agreement, dated as of February 15, 2007, by and between the Company and Inspire Pharmaceuticals, Inc.
10.28[22H]	Trademark License Agreement, dated as of February 15, 2007, by and between the Company and Inspire Pharmaceuticals, Inc.
10.29[22H]	Supply Agreement, dated as of February 15, 2007, by and between the Company and Inspire Pharmaceuticals, Inc.
10.30[22HH]	Change in Control Agreement for S. Kumar Chandrasekaran adopted by InSite Vision Incorporated on May 2, 2007.
10.31[23]	Purchase and Sale Agreement, dated as of February 21, 2008, by and between Azithromycin Royalty Sub LLC and the Company.
10.32[23]	Note Purchase Agreement, dated as of February 21, 2008, by and among Azithromycin Royalty Sub LLC, the Company and the purchasers named therein.
10.33[23]	Indenture, dated as of February 21, 2008, by and between Azithromycin Royalty Sub LLC and U.S. Bank National Association.
10.34[23]	Pledge and Security Agreement made by the Company to U.S. Bank National Association, as Trustee, dated February 21, 2008.
10.35[23]	Residual License Agreement by and between Azithromycin Royalty Sub LLC and the Company dated February 21, 2008.
10.36[24]	InSite Vision Incorporated Annual Bonus Plan.
10.37[25]	InSite Vision Incorporated Severance Plan.
10.38 [HH]	Offer letter, by and between the Company and Louis Drapeau, dated October 31, 2008.

Number	Exhibit Table
10.39[HH]	Offer letter, by and between the Company and Timothy Ruane, dated December 1, 2010.
21.1	List of Subsidiaries.
23.1	Consent of Burr Pilger Mayer, Inc., Independent Registered Public Accounting Firm.
24.1	Reference is hereby made to the Power of Attorney included on the signature page to this Annual Report on Form 10-K.
31.1	Certification of Principal Executive Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
31.2	Certification of Principal Financial Officer pursuant to Rules 13a-14(a) and 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
32.1	Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

1. Incorporated by reference to exhibits in the Company's Annual Report on Form 10-K for the year ended December 31, 1993.
2. Incorporated by reference to exhibits in the Company's Registration Statement on Form S-3 (Registration No. 333-36673) as filed with the Securities and Exchange Commission on September 29, 1997.
3. Incorporated by reference to an exhibit in Amendment No. 1 the Company's Registration Statement on Form S-1 (Registration No. 33-68024) as filed with the Securities and Exchange Commission on September 16, 1993.
4. Incorporated by reference to an exhibit to the Company's Registration Statement on Form S-3 (file Number 333-126084) as filed with the Securities and Exchange Commission on June 23, 2005.
5. Incorporated by reference to an exhibit in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.
6. Incorporated by reference to an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2006.
7. Incorporated by reference to an exhibit in the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on June 6, 2008.
8. Incorporated by reference to an exhibit in the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on October 19, 2007.
9. Incorporated by reference to exhibits to the Company's Registration Statement on Form S-8 (Registration No. 333-60057) as filed with the Securities and Exchange Commission on July 28, 1998.
10. Incorporated by reference to an exhibit in the Company's Registration Statement on Form S-1 (Registration No. 33-68024) as filed with the Securities and Exchange Commission on August 27, 1993.
11. Incorporated by reference to an exhibit in the Company's Annual Report on Form 10-K for the year ended December 31, 1993.
12. Incorporated by reference to an exhibit to Amendment No. 1 the Company's Registration Statement on Form S-1 (Registration No. 33-68024) as filed with the Securities and Exchange Commission on September 16, 1993.
13. Incorporated by reference to an exhibit to the Company's Annual Report on Form 10-K for the year ended December 31, 1996.
14. Incorporated by reference to an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 1996.
15. Incorporated by reference to an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2001.
16. Incorporated by reference to an exhibit to the Company's Annual Report of Form 10-K for the year ended December 31, 2001.
17. Incorporated by reference to an exhibit to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on January 14, 2004.

18. Incorporated by reference to an exhibit to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on March 29, 2004.
19. Incorporated by reference to an exhibit to the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on October 11, 2005 (File Number 001-14207).
20. Incorporated by reference to an exhibit to the Company's Registration Statement on Form S-3 filed with the Securities and Exchange Commission on February 10, 2006 (File Number 333-131774).
21. Incorporated by reference to an exhibit to the Company's Registration Statement on Form S-3 filed with the Securities and Exchange Commission on October 13, 2006 (File Number 333-137994).
22. Incorporated by reference to an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2007.
23. Incorporated by reference to an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2008.
24. Incorporated by reference to an exhibit to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2008.
25. Incorporated by reference to an exhibit in the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on April 29, 2009.
26. Incorporated by reference to an exhibit in the Company's Current Report on Form 8-K filed with the Securities and Exchange Commission on November 30, 2010.

H Confidential treatment has been granted with respect to certain portions of this agreement.

HH Management contract or compensatory plan.

Exhibit 21.1

Subsidiaries of InSite Vision Incorporated

Name	Place of Incorporation
Azithromycin Royalty Sub, LLC	Delaware
Ophthalmic Solutions, Inc.	Delaware
InSite Vision, Ltd.	United Kingdom

Exhibit 23.1

Consent of Burr Pilger Mayer, Inc., Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statements on Forms S-3 (No. 333-38266, No. 333-54912, No. 333-116973, No. 333-126084, No. 333-130248, No. 333-131744 and No. 333-137994) and the Registration Statements on Forms S-8 (No. 33-75268, No. 33-80662, No. 33-93394, No. 333-29801, No. 333-60057, No. 333-79789, No. 333-43504, No. 333-72098, No. 333-117193, No. 333-126083, No. 333-133010 and No. 333-143016) of InSite Vision Incorporated of our report dated March 4, 2011, with respect to the consolidated financial statements which appear in this Form 10-K.

/s/ Burr Pilger Mayer, Inc.

San Francisco, California
March 4, 2011

EXHIBIT 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Timothy Ruane, certify that:

1. I have reviewed this annual report on Form 10-K of InSite Vision Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonable likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: March 4, 2011

/s/ TIMOTHY RUANE

Timothy Ruane
Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Louis Drapeau, certify that:

1. I have reviewed this annual report on Form 10-K of InSite Vision Incorporated;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal controls over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonable likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: March 4, 2011

/s/ LOUIS DRAPEAU

Louis Drapeau
Chief Financial Officer
(Principal Financial Officer)

EXHIBIT 32.1

CERTIFICATION OF
PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Timothy Ruane, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Annual Report of InSite Vision Incorporated on Form 10-K for the annual period ended December 31, 2010 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended and that information contained in such Annual Report of InSite Vision Incorporated on Form 10-K fairly presents, in all material respects, the financial condition and results of operations of InSite Vision Incorporated.

By: /s/ TIMOTHY RUANE
Name: **Timothy Ruane**
Title: **Chief Executive Officer**
(Principal Executive Officer)
Date: **March 4, 2011**

CERTIFICATION OF
PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Louis Drapeau, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Annual Report of InSite Vision Incorporated on Form 10-K for the annual period ended December 31, 2010 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended and that information contained in such Annual Report of InSite Vision Incorporated on Form 10-K fairly presents, in all material respects, the financial condition and results of operations of InSite Vision Incorporated.

By: /s/ LOUIS DRAPEAU
Name: **Louis Drapeau**
Title: **Chief Financial Officer**
(Principal Financial Officer)
Date: **March 4, 2011**

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Corporate and Stockholder Information

Management Team

Timothy Ruane
Chief Executive Officer

Louis Drapeau
Vice President, Chief Financial Officer

Lyle M. Bowman, Ph.D.
Vice President, Development

Kamran Hosseini, M.D., Ph.D.
Vice President, Clinical Affairs and
Chief Medical Officer

Surendra Patel
Vice President, Operations

Board of Directors

Evan S. Melrose, M.D.
Chairman of the Board
Managing Director, PTV Sciences

Rick D. Anderson
Managing Director, PTV Sciences

Timothy P. Lynch
General Partner, Stonepine Capital, LLC

Timothy McInerney
Partner, Riverbank Capital Securities

Robert O'Holla
President, R.O.H Consulting, LLC

Timothy Ruane
Chief Executive Officer

Anthony J. Yost
Vice President of Sales and
Marketing, PacifiCord

Corporate Headquarters

965 Atlantic Avenue | Alameda, CA 94501
tel: 510.865.8800 | *fax:* 510.865.5700
mail@insite.com
www.insitevision.com

Corporate Counsel

Jones Day
Palo Alto, California

Independent Auditors

Burr Pilger Mayer, Inc.
San Francisco, California

Transfer Agent

American Stock Transfer
& Trust Company, LLC
Barry S. Rosenthal
Vice President
6201 15th Avenue | Brooklyn, NY 11219
tel: 718.921.8380 | *fax:* 718.765.8718
www.amstock.com

Market Information

InSite Vision's common stock is listed on the Over-the-Counter Bulletin Board (OTCBB) under the symbol INSV and the closing sale price for its common stock was $0.81 on April 11, 2011.

InSite Vision has not paid any cash dividends on its common stock and does not intend to do so in the foreseeable future.

All exhibits to the Company's Annual Report on Form 10-K are briefly described in the exhibit table of that form, a copy of which is included herewith. The Company will provide stockholders with copies of any exhibits to the Company's Annual Report upon receipt of a written request at Investor Relations, 965 Atlantic Avenue, Alameda, California 94501 or by telephone to (510) 865-8800.

This Annual Report, including the letter from our Chief Executive Officer, contains certain forward-looking statements that involve numerous risks and uncertainties, such as statements of our plans, beliefs, objectives, expectations and intentions. Actual results or events could differ materially from those discussed herein. Factors that could cause or contribute to such differences include those discussed under "Risk Factors" and elsewhere in our Annual Report on Form 10-K included herewith and our other reports filed with the Securities and Exchange Commission. The cautionary statements made in these documents should be read as applicable to all related forward-looking statements wherever they appear in this document and the enclosures included herewith. Readers are cautioned not to place undue reliance on these forward-looking statements, which are based on the limited information currently available to us and are subject to change. Although any such forward-looking statements or projections and the factors influencing them will likely change, we undertake no obligation to update any forward-looking statements to reflects events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

InSite Vision Incorporated

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