

PROSPECT CAPITAL CORP  
 Form 40-17G  
 October 21, 2008

**COPY OF BINDER**

AIG EXECUTIVE LIABILITY<sup>SM</sup>

Insurance provided by the following member of American International Group, Inc.  
 National Union Fire Insurance Company of Pittsburgh, Pa.

A capital stock company

POLICY NUMBER: 00-669-12-00

REPLACEMENT OF POLICY NUMBER: 00-695-93-31

**INVESTMENT COMPANY BLANKET BOND**

**DECLARATIONS:**

ITEM 1. Name of Insured (herein called Insured): PROSPECT ENERGY CORPORATION LLC

Principal Address: 10 EAST 40TH STREET  
 NEW YORK, NY 10016

ITEM 2. Bond Period: from 12:01 a.m. July 30, 2008 to July 30, 2009, the effective date of the termination or cancellation of this bond, standard time at the Principal Address as to each of said dates.

ITEM 3. Limit of Liability - Subject to Sections 9, 10 and 12 hereof,

	Single Loss Limit of Liability	Single Loss Deductible
Insuring Agreement A (Fidelity)-	\$1,000,000	\$10,000
Insuring Agreement B (Audit Expense)-	\$25,000	\$5,000
Insuring Agreement C (On Premises)-	\$1,000,000	\$10,000
Insuring Agreement D (In Transit)-	\$1,000,000	\$10,000
Insuring Agreement E (Forgery or Alteration)-	\$1,000,000	\$10,000
Insuring Agreement F (Securities)-	\$1,000,000	\$10,000
Insuring Agreement G (Counterfeit Currency)-	\$1,000,000	\$10,000
Insuring Agreement H (Stop Payment)-	\$25,000	\$5,000
Insuring Agreement I (Uncollectible Items of Deposit)-	\$25,000	\$5,000
Insuring Agreement J (Computer Systems)-	\$1,000,000	\$10,000
Insuring Agreement K (Voice Initiated Transfer Fraud)-	\$1,000,000	\$10,000

If "Not Covered" is inserted above opposite any specified Insuring Agreement or Coverage, such Insuring Agreement or Coverage and any other reference thereto in this bond shall be deemed to be deleted therefrom.

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ITEM 4. Offices or Premises Covered-Offices acquired or established subsequent to the effective date of this bond are covered according to the terms of General Agreement A. All the Insured's offices or premises in existence at the time this bond becomes effective are covered under this bond except the offices or premises located as follows: No Exceptions

ITEM 5. The liability of the Underwriter is subject to the terms of the following riders attached thereto: Rider #1, #2, #3

ITEM 6. The Insured by the acceptance of this bond gives to the Underwriter terminating or canceling prior bond(s) or policy(ies) No.(s) 695-93-31 such termination or cancellation to be effective as of the time this bond becomes effective.

PREMIUM: \$5,795

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IN WITNESS WHEREOF, the Insurer has caused this policy to be signed on the Declarations by its President, a Secretary and its duly authorized representative.

PRESIDENT

AUTHORIZED REPRESENTATIVE

SECRETARY

COUNTERSIGNATURE

DATE

COUNTERSIGNED AT

AON RISK SERVICES INC OF NY  
199 Water Street  
NEW YORK, NY 10038

### **INVESTMENT COMPANY BLANKET BOND**

The Underwriter, in consideration of an agreed premium, and subject to the Declarations made a part hereof, the General Agreements, Conditions and Limitations and other terms of this bond, agrees with the Insured, in accordance with the Insuring Agreements hereof to which an amount of insurance is applicable as set forth in Item 3 of the Declarations and with respect to loss sustained by the Insured at any time but discovered during the Bond Period, to indemnify and hold harmless the Insured for:

#### **INSURING AGREEMENTS**

##### **(A) FIDELITY**

Loss resulting from any dishonest or fraudulent act(s), including Larceny or Embezzlement committed by an Employee, committed anywhere and whether committed alone or in collusion with others, including loss of Property resulting from such acts of an Employee, which Property is held by the Insured for any purpose or in any capacity and whether so held gratuitously or not and whether or not the Insured is liable therefor.

Dishonest or fraudulent act(s) as used in this Insuring Agreement shall mean only dishonest or fraudulent act(s) committed by such Employee with the manifest intent:

- (a) to cause the Insured to sustain such loss; and
- (b) to obtain financial benefit for the Employee, or for any other person or organization intended by the Employee to receive such benefit, other than salaries, commissions, fees, bonuses, promotions, awards, profit sharing, pensions or other employee benefits earned in the normal course of employment.

##### **(B) AUDIT EXPENSE**

Expense incurred by the Insured for that part of the costs of audits or examinations required by any governmental regulatory authority to be conducted either by such authority or by an independent accountant by reason of the discovery of loss sustained by the Insured through any dishonest or fraudulent act(s), including Larceny or Embezzlement of any of the Employees.

The total liability of the Underwriter for such expense by reason of such acts of any Employee or in which such Employee is concerned or implicated or with respect to any one audit or examination is limited to the amount stated opposite Audit Expense in Item 3 of the Declarations; it being understood, however, that such expense shall be deemed to be a loss sustained by the Insured through any dishonest or fraudulent act(s), including Larceny or Embezzlement of one or more of the Employees and the liability under this paragraph shall be in addition to the Limit of liability stated in Insuring Agreement (A) in Item 3 of the Declarations.

##### **(C) ON PREMISES**

Loss of Property (occurring with or without negligence or violence) through robbery, burglary, Larceny, theft, holdup, or other fraudulent means, misplacement, mysterious unexplainable disappearance, damage thereto or destruction thereof, abstraction or removal from the possession, custody or control of the Insured, and loss of subscription, conversion, redemption or deposit privileges through the misplacement or loss of Property, while the Property is (or is supposed or believed by the Insured to be) lodged or deposited within any offices or premises located anywhere, except in an office listed in Item 4 of the Declarations or amendment thereof or in the mail or with a carrier for hire other than an armored motor vehicle company, for the purpose of transportation.

(1) Loss of or damage to, furnishings, fixtures, stationery, supplies or equipment, within any of the Insured's offices covered under this bond caused by Larceny or theft in, or by burglary, robbery or holdup of such office, or attempt thereat, or by vandalism or malicious mischief; or

(2) loss through damage to any such office by Larceny or theft in, or by burglary, robbery or holdup of such office or attempt thereat, or to the interior of any such office by vandalism or malicious mischief provided, in any event, that the Insured is the owner of such offices, furnishings, fixtures, stationery, supplies or equipment or is legally liable for such loss or damage, always excepting, however, all loss or damage through fire.

(D) IN TRANSIT

Loss of Property (occurring with or without negligence or violence) through robbery, Larceny, theft, holdup, misplacement, mysterious unexplainable disappearance, being lost or otherwise made away with, damage thereto or destruction thereof, and loss of subscription, conversion, redemption or deposit privileges through the misplacement or loss of Property, while the Property is in transit anywhere in the custody of any person or persons acting as messenger, except while in the mail or with a carrier for hire, other than an armored motor vehicle company, for the purpose of transportation, such transit to begin immediately upon receipt of such Property by the transporting person or persons, and to end immediately upon delivery thereof at destination.

Loss through FORGERY or ALTERATION of, on or in any bills of exchange, checks, drafts, acceptances, certificates of deposit, promissory notes, or other written promises, orders or directions to pay sums certain in money, due bills, money orders, warrants, orders upon public treasuries, letters of credit, written instructions, advices or applications directed to the Insured, authorizing or acknowledging the transfer, payment, delivery or receipt of funds or Property, which instructions or advices or applications purport to have been signed or endorsed by any customer of the Insured, shareholder or subscriber to shares, whether certificated or uncertificated, of any Investment Company or by any financial or banking institution or stockbroker but which instructions, advices or applications either bear the forged signature or endorsement or have been altered without the knowledge and consent of such customer, shareholder or subscriber to shares, whether certificated or uncertificated, of an Investment Company, financial or banking institution or stockbroker, withdrawal orders or receipts for the withdrawal of funds or Property, or receipts or certificates of deposit for Property and bearing the name of the Insured as issuer, or of another Investment Company for which the Insured acts as agent, excluding, however, any loss covered under Insuring Agreement (F) hereof whether or not coverage for Insuring Agreement (F) is provided for in the Declarations of this bond.

Any check or draft (a) made payable to a fictitious payee and endorsed in the name of such fictitious payee or (b) procured in a transaction with the maker or drawer thereof or with one acting as an agent of such maker or drawer or anyone impersonating another and made or drawn payable to the one so impersonated and endorsed by anyone other than the one impersonated, shall be deemed to be forged as to such endorsement.

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(F) SECURITIES

Loss sustained by the Insured, including loss sustained by reason of a violation of the constitution, by-laws, rules or regulations of any Self Regulatory Organization of which the Insured is a member or which would have been imposed upon the Insured by the constitution, by-laws, rules or regulations of any Self Regulatory Organization if the Insured had been a member thereof,

Securities, documents or other written instruments shall be deemed to mean original (including original counterparts) negotiable or non-negotiable agreements which in and of themselves represent an equitable interest, ownership, or debt, including an assignment thereof which instruments are in the ordinary course of business, transferable by delivery of such agreements with any necessary endorsement or assignment.

The word "counterfeited" as used in this Insuring Agreement shall be deemed to mean any security, document or other written instrument which is

(1) through the Insured's having, in good faith and in the course of business, whether for its own account or for the account of others, in any representative, fiduciary, agency or any other capacity, either gratuitously or otherwise, purchased or otherwise acquired, accepted or received, or sold or delivered, or given any value, extended any credit or assumed any liability, on the faith of, or otherwise acted upon, any securities, documents or other written instruments which prove to have been

(a) counterfeited, or

(b) forged as to the signature of any maker, drawer, issuer, endorser, assignor, lessee, transfer agent or registrar, acceptor, surety or guarantor or as to the signature of any person signing in any other capacity, or

(c) raised or otherwise altered, or lost, or stolen, or

(2) through the Insured's having, in good faith and in the course of business, guaranteed in writing or witnessed any signatures whether for valuable consideration or not and whether or not such guaranteeing or witnessing is ultra vires the Insured, upon any transfers, assignments, bills of sale, powers of attorney, guarantees, endorsements or other obligations upon or in connection with any securities, documents or other written instruments and which pass or purport to pass title to such securities, documents or other written instruments; EXCLUDING, losses caused by FORGERY or ALTERATION of, on or in those instruments covered under Insuring Agreement (E) hereof.

intended to deceive and to be taken for an original.

Mechanically produced facsimile signatures are treated the same as handwritten signatures.

(G) COUNTERFEIT CURRENCY

Loss through the receipt by the Insured, in good faith, of any counterfeited money orders or altered paper currencies or coin of the United States of America or Canada issued or purporting to have been issued by the United States of America or Canada or issued pursuant to a United States of America or Canadian statute for use as currency.

(H) STOP PAYMENT

Loss against any and all sums which the Insured shall become obligated to pay by reason of the Liability imposed upon the Insured by law for damages:

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For having either complied with or failed to comply with any written notice of any customer, shareholder or subscriber of the Insured or any Authorized Representative of such customer, shareholder or subscriber to stop payment of any check or draft made or drawn by such customer, shareholder or subscriber or any Authorized Representative of such customer, shareholder or subscriber, or

For having refused to pay any check or draft made or drawn by any customer, shareholder or subscriber of the Insured or any Authorized Representative of such customer, shareholder or subscriber.

(I) UNCOLLECTIBLE ITEMS OF DEPOSIT

loss resulting from any Item of Deposit processed through an Automated Clearing House which is reversed by the customer, shareholder or subscriber and deemed uncollectible by the Insured.

Loss includes dividends and interest accrued not to exceed 15% of the Uncollectible Items which are deposited.

This Insuring Agreement applies to all Mutual Funds with "exchange privileges" if all Fund(s) in the exchange program are insured by a National Union Fire Insurance Company of Pittsburgh, PA for Uncollectible Items of Deposit. Regardless of the number of transactions between Fund(s), the minimum number of days of deposit within the Fund(s) before

Loss resulting from payments of dividends or fund shares, or withdrawals permitted from any customer's, shareholder's or subscriber's account based upon Uncollectible Items of Deposit of a customer, shareholder or subscriber credited by the Insured or the Insured's agent to such customer's, shareholder's or subscriber's Mutual Fund Account; or

withdrawal as declared in the Fund(s) prospectus shall begin from the date a deposit was first credited to any Insured Fund(s).

## GENERAL AGREEMENTS

### A. ADDITIONAL OFFICES OR EMPLOYEES-CONSOLIDATION OR MERGER-NOTICE

1. If the Insured shall, while this bond is in force, establish any additional office or offices, such office or offices shall be automatically covered hereunder from the dates of their establishment, respectively. No notice to the Underwriter of an increase during any premium period in the number of offices or in the number of Employees at any of the offices covered hereunder need be given and no additional premium need be paid for the remainder of such premium period.

2. If an Investment Company, named as Insured herein, shall, while this bond is in force, merge or consolidate with, or purchase the assets of another institution, coverage for such acquisition shall apply automatically from the date of acquisition. The Insured shall notify the Underwriter of such acquisition within 60 days of said date, and an additional premium shall be computed only if such acquisition involves additional offices or employees.

### B. WARRANTY

No statement made by or on behalf of the Insured, whether contained in the application or otherwise, shall be deemed to be a warranty of anything except that it is true to the best of the knowledge and belief of the person making the statement.

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### C. COURT COSTS AND ATTORNEYS' FEES (Applicable to all Insuring Agreements or Coverages now or hereafter forming part of this bond)

The Underwriter will indemnify the Insured against court costs and reasonable attorneys' fees incurred and paid by the Insured in defense, whether or not successful, whether or not fully litigated on the merits and whether or not settled of any suit or legal proceeding brought against the Insured to enforce the Insured's liability or alleged liability on account of any loss, claim or damage which, if established against the Insured, would constitute a loss sustained by the Insured covered under the terms of this bond provided, however, that with respect to Insuring Agreement (A) this indemnity shall apply only in the event that

(1) an Employee admits to being guilty of any dishonest or fraudulent act(s), including Larceny or Embezzlement; or

The Insured shall promptly give notice to the Underwriter of any such suit or legal proceeding and at the request of the Underwriter shall furnish it with copies of all pleadings and other papers therein. At the Underwriter's election the Insured shall permit the Underwriter to conduct the defense of such suit or legal proceeding, in the Insured's name, through attorneys of the Underwriter's selection. In such event, the Insured shall give all reasonable information and assistance which the Underwriter shall deem necessary to the proper defense of such suit or legal proceeding.

If the amount of the Insured's liability or alleged liability is greater than the amount recoverable under this bond, or if a Deductible Amount is applicable, or both, the liability of the Underwriter under this General Agreement is limited to the proportion of court costs and attorneys' fees incurred and paid by the Insured or by the Underwriter that the amount recoverable under this bond bears to the total of such

(2) an Employee is adjudicated to be guilty of any dishonest or fraudulent act(s), including Larceny or Embezzlement;

(3) in the absence of (1) or (2) above an arbitration panel agrees, after a review of an agreed statement of facts, that an Employee would be found guilty of dishonesty if such Employee were prosecuted.

amount plus the amount which is not so recoverable. Such indemnity shall be in addition to the Limit of Liability for the applicable Insuring Agreement or Coverage.

D. FORMER EMPLOYEE

Acts of an Employee, as defined in this bond, are covered under Insuring Agreement (A) only while the Employee is in the Insured's employ. Should loss involving a former Employee of the Insured be discovered subsequent to the termination of employment, coverage would still apply under Insuring Agreement (A) if the direct proximate cause of the loss occurred while the former Employee performed duties within the scope of his/her employment.

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**THE FOREGOING INSURING AGREEMENTS AND GENERAL AGREEMENTS ARE SUBJECT TO THE FOLLOWING CONDITIONS AND LIMITATIONS:**

SECTION 1. DEFINITIONS

The following terms, as used in this bond, shall have the respective meanings stated in this Section:

(a) "Employee" means:

(1) any of the Insured's officers, partners, or employees, and

(2) any of the officers or employees of any predecessor of the Insured whose principal assets are acquired by the Insured by consolidation or merger with, or purchase of assets or capital stock of such predecessor. and

(3) attorneys retained by the Insured to perform legal services for the Insured and the employees of such attorneys while such attorneys or the employees of such attorneys are performing such services for the Insured, and

(4) guest students pursuing their studies or duties in any of the Insured's offices, and

(5) directors or trustees of the Insured, the investment advisor, underwriter (distributor), transfer agent, or shareholder

(6) any individual or individuals assigned to perform the usual duties of an employee within the premises of the Insured, by contract, or by any agency furnishing temporary personnel on a contingent or part-time basis, and

(7) each natural person, partnership or corporation authorized by written agreement with the Insured to perform services as electronic data processor of checks or other accounting records of the Insured, but excluding any such processor who acts as transfer agent or in any other agency capacity in issuing checks, drafts or securities for the Insured, unless included under Sub-section (9) hereof, and

(8) those persons so designated in Section 15, Central Handling of Securities, and

(9) any officer, partner or Employee of

a) an investment advisor,

b) an underwriter (distributor),

c) a transfer agent or shareholder accounting record-keeper, or

accounting record keeper, or administrator authorized by written agreement to keep financial and/or other required records, but only while performing acts coming within the scope of the usual duties of an officer or employee or while acting as a member of any committee duly elected or appointed to examine or audit or have custody of or access to the Property of the Insured, and

d) an administrator authorized by written agreement to keep financial and/or other required records,

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for an Investment Company named as Insured while performing acts coming within the scope of the usual duties of an officer or Employee of any Investment Company named as Insured herein, or while acting as a member of any committee duly elected or appointed to examine or audit or have custody of or access to the Property of any such Investment Company, provided that only Employees or partners of a transfer agent, shareholder accounting record-keeper or administrator which is an affiliated person as defined in the Investment Company Act of 1940, of an Investment Company named as Insured or is an affiliated person of the adviser, underwriter or administrator of such Investment Company, and which is not a bank, shall be included within the definition of Employee.

Each employer of temporary personnel or processors as set forth in Sub-Sections (6) and of Section 1(a) and their partners, officers and employees shall collectively be deemed to be one person for all the purposes of this bond, excepting, however, the last paragraph of Section 13.

Brokers, or other agents under contract or representatives of the same general character shall not be considered Employees.

(b) "Property" means money (i.e.. currency, coin, bank notes, Federal Reserve notes), postage and revenue stamps, U.S. Savings Stamps, bullion, precious metals of all kinds and in any form and articles made therefrom, jewelry, watches, necklaces, bracelets, gems, precious and semi-

precious stones, bonds, securities, evidences of debts, debentures, scrip, certificates, interim receipts, warrants, rights, puts, calls, straddles, spreads, transfers, coupons, drafts, bills of exchange, acceptances, notes, checks, withdrawal orders, money orders, warehouse receipts, bills of lading, conditional sales contracts, abstracts of title, insurance policies, deeds, mortgages under real estate and/or chattels and upon interests therein, and assignments of such policies, mortgages and instruments, and other valuable papers, including books of account and other records used by the Insured in the conduct of its business, and all other instruments similar to or in the nature of the foregoing including Electronic Representations of such instruments enumerated above (but excluding all data processing records) in which the Insured has an interest or in which the Insured acquired or should have acquired an interest by reason of a predecessor's declared financial condition at the time of the Insured's consolidation or merger with, or purchase of the principal assets of, such predecessor or which are held by the Insured for any purpose or in any capacity and whether so held by the Insured for any purpose or in any capacity and whether so held gratuitously or not and whether or not the Insured is liable therefor.

(c) "Forgery" means the signing of the name of another with intent to deceive; it does not include the signing of one's own name with or without authority, in any capacity, for any purpose.

(d) "Larceny and Embezzlement" as it applies to any named Insured means those acts as set forth in Section 37 of the Investment Company Act of 1940.

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(e) "Items of Deposit" means any one or more checks and drafts. Items of Deposit shall not be deemed uncollectible until the Insured's collection procedures have failed.

(e) loss resulting from the complete or partial non-payment of, or default upon, any loan or transaction in the nature of, or amounting to, a loan made by or obtained from the Insured or any of its partners, directors or Employees, whether authorized



SECTION 2. EXCLUSIONS

THIS BOND DOES NOT COVER:

(a) loss effected directly or indirectly by means of forgery or alteration of, on or in any instrument, except when covered by Insuring Agreement (A), (E), (F) or (G).

(b) loss due to riot or civil commotion outside the United States of America and Canada; or loss due to military, naval or usurped power, war or insurrection unless such loss occurs in transit in the circumstances recited in Insuring Agreement (D), and unless, when such transit was initiated, there was no knowledge of such riot, civil commotion, military, naval or usurped power, war or insurrection on the part of any person acting for the Insured in initiating such transit.

(c) loss, in time of peace or war, directly or indirectly caused by or resulting from the effects of nuclear fission or fusion or radioactivity; provided, however, that this paragraph shall not apply to loss resulting from industrial uses of nuclear energy.

(d) loss resulting from any wrongful act or acts of any person who is a member of the Board of Directors of the Insured or a member of any equivalent body by whatsoever name known unless such person is also an Employee or an elected official, partial owner or partner of the Insured in some other capacity, nor, in any event, loss resulting from the act or acts of any person while acting in the capacity of a member of such Board or equivalent body.

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(h) potential income, including but not limited to interest and dividends, not realized by the Insured because of a loss covered under this bond, except as included under Insuring Agreement (I).

(i) all damages of any type for which the Insured is legally liable, except direct compensatory damages arising from a loss covered under this bond.

(j) loss through the surrender of Property away from an office of the Insured as a result of a threat

(1) to do bodily harm to any person, except loss of Property in transit in the custody of any person acting as messenger provided that when such transit was initiated there was no knowledge by the Insured of any such threat, or

(2) to do damage to the premises or Property of the Insured, except when covered under Insuring

or unauthorized and whether procured in good faith or through trick, artifice, fraud or false pretenses. unless such loss is covered under Insuring Agreement (A), (E) or (F).

(f) loss resulting from any violation by the Insured or by any Employee

(1) of law regulating (a) the issuance, purchase or sale of securities, (b) securities transactions upon Security Exchanges or over the counter market, (c) Investment Companies, or (d) Investment Advisors, or

(2) of any rule or regulation made pursuant to any such law, unless such loss, in the absence of such laws, rules or regulations, would be covered under Insuring Agreements (A) or (E).

(g) loss of Property or loss of privileges through the misplacement or loss of Property as set forth in Insuring Agreement (C) or (D) while the Property is in the custody of any armored motor vehicle company, unless such loss shall be in excess of the amount recovered or received by the Insured under (a) the Insured's contract with said armored motor vehicle company, (b) insurance carried by said armored motor vehicle company for the benefit of users of its service, and (c) all other insurance and indemnity in force in whatsoever form carried by or for the benefit of users of said armored motor vehicle company's service, and then this bond shall cover only such excess.

(m) any loss resulting from Uncollectible Items of Deposit which are drawn from a financial institution outside the fifty states of the United States of America, District of Columbia, and territories and possessions of the United States of America, and Canada.

SECTION 3. ASSIGNMENT OF RIGHTS

This bond does not afford coverage in favor of any Employers of temporary personnel or of processors as set forth in sub-sections (6) and (7) of Section 1(a) of this bond, as aforesaid, and upon payment to the Insured by the Underwriter on account of any loss through dishonest or fraudulent act(s) including Larceny or Embezzlement committed by any of the partners, officers or employees of such Employers, whether acting alone or in collusion with others, an assignment of such of the Insured's rights and causes of action as it may have against such Employers by

Agreement (A).

(k) all costs, fees and other expenses incurred by the Insured in establishing the existence of or amount of loss covered under this bond unless such indemnity is provided for under Insuring Agreement (B).

(l) loss resulting from payments made or withdrawals from the account of a customer of the Insured, shareholder or subscriber to shares involving funds erroneously credited to such account, unless such payments are made to or withdrawn by such depositor or representative of such person, who is within the premises of the drawee bank of the Insured or within the office of the Insured at the time of such payment or withdrawal or unless such payment is covered under Insuring Agreement (A).

reason of such acts so committed shall, to the extent of such payment, be given by the Insured to the Underwriter, and the Insured shall execute all papers necessary to secure to the Underwriter the rights herein provided for.

#### SECTION 4. LOSS -NOTICE -PROOF-LEGAL PROCEEDINGS

This bond is for the use and benefit only of the Insured named in the Declarations and the Underwriter shall not be liable hereunder for loss sustained by anyone other than the Insured unless the Insured, in its sole discretion and at its option, shall include such loss in the Insured's proof of loss. At the earliest practicable moment after discovery of any loss hereunder the Insured shall give the Underwriter written notice thereof and shall also within six months after such discovery furnish to the Underwriter affirmative proof of loss with full particulars.

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If claim is made under this bond for loss of securities or shares, the Underwriter shall not be liable unless each of such securities or shares is identified in such proof of loss by a certificate or bond number or, where such securities or shares are uncertificated, by such identification means as agreed to by the Underwriter. The Underwriter shall have thirty days after notice and proof of loss within which to investigate the claim, but where the loss is clear and undisputed, settlement shall be made within forty-eight hours; and this shall apply notwithstanding the loss is made up wholly or in part of securities of which duplicates may be obtained. Legal proceedings for recovery of any loss hereunder shall not be brought prior to the expiration of sixty days after such proof of loss is filed with the Underwriter nor after the expiration of twenty-four months from the discovery of such loss, except that any action or proceeding to recover hereunder on account of any judgment against the Insured in any suit mentioned in General Agreement C or to recover attorneys' fees paid in any such suit, shall be begun within twenty-four months from the date upon which the judgment in such suit shall become final. If any limitation embodied in this bond is prohibited by any law controlling the construction hereof, such limitation shall be deemed to be amended so as to be equal to the minimum period of limitation permitted by such law.

Discovery occurs when the Insured

(a) becomes aware of facts, or

#### SECTION 5. VALUATION OF PROPERTY

The value of any Property, except books of accounts or other records used by the Insured in the conduct of its business, for the loss of which a claim shall be made hereunder, shall be determined by the average market value of such Property on the business day next preceding the discovery of such loss; provided, however, that the value of any Property replaced by the Insured prior to the payment of claim therefor shall be the actual market value at the time of replacement; and further provided that in case of a loss or misplacement of interim certificates, warrants, rights, or other securities, the production which is necessary to the exercise of subscription, conversion, redemption or deposit privileges, the value thereof shall be the market value of such privileges immediately preceding the expiration thereof if said loss or misplacement is not discovered until after their expiration. If no market price is quoted for such Property or for such privileges, the value shall be fixed by agreement between the parties or by arbitration.

In case of any loss or damage to Property consisting of books of accounts or other records used by the Insured in the conduct of its business, the Underwriter shall be liable under this bond only if such books or records are actually reproduced and then for not more than the cost of blank books, blank pages or other materials plus the cost of labor for the actual transcription or copying of data which shall have been furnished by the Insured in order to reproduce such books and other records.

(b) receives written notice of an actual or potential claim by a third party which alleges that the Insured is liable under circumstance which would cause a reasonable person to assume that a loss covered by the bond has been or will be incurred even though the exact amount or details of loss may not be then known.

#### SECTION 6. VALUATION OF PREMISES AND FURNISHINGS

In case of damage to any office of the Insured, or loss of or damage to the furnishings, fixtures, stationery, supplies, equipment, safes or vaults therein, the Underwriter shall not be liable for more than the actual cash value thereof, or for more than the actual cost of their replacement or repair. The Underwriter may, at its election, pay such actual cash value or make such replacement or repair. If the Underwriter and the Insured cannot agree upon such cash value or such cost of replacement or repair, such shall be determined by arbitration.

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#### SECTION 7. LOST SECURITIES

If the Insured shall sustain a loss of securities the total value of which is in excess of the limit stated in Item 3 of the Declarations of this bond, the liability of the Underwriter shall be limited to payment for, or duplication of, securities having value equal to the limit stated in Item 3 of the Declarations of this bond.

If the Underwriter shall make payment to the Insured for any loss of securities, the Insured shall thereupon assign to the Underwriter all of the Insured's rights, title and interests in and to said securities.

With respect to securities the value of which do not exceed the Deductible Amount (at the time of the discovery of the loss) and for which the Underwriter may at its sole discretion and option and at the request of the Insured issue a Lost Instrument Bond or Bonds to effect replacement thereof, the Insured will pay the usual premium charged therefor and will indemnify the Underwriter against all loss or expense that the Underwriter may sustain because of the issuance of such Lost Instrument Bond or Bonds.

With respect to securities the value of which exceeds the Deductible Amount (at the time of discovery of the loss) and for which the Underwriter may issue or arrange for the issuance of a Lost Instrument Bond or Bonds to effect replacement thereof, the Insured agrees that it will pay as premium therefor a proportion of the usual premium charged therefor, said proportion being equal to the percentage that the Deductible Amount bears to the value of the securities upon discovery of the loss, and that it will indemnify the issuer of said Lost Instrument Bond or Bonds against all loss and expense that is not recoverable from the Underwriter

#### SECTION 8. SALVAGE

In case of recovery, whether made by the Insured or by the Underwriter, on account of any loss in excess of the Limit of Liability hereunder plus the Deductible Amount applicable to such loss from any source other than suretyship, insurance, reinsurance, security or indemnity taken by or for the benefit of the Underwriter, the net amount of such recovery, less the actual costs and expenses of making same, shall be applied to reimburse the Insured in full for the excess portion of such loss, and the remainder, if any, shall be paid first in reimbursement of the Underwriter and thereafter in reimbursement of the Insured for that part of such loss within the Deductible Amount. The Insured shall execute all necessary papers to secure to the Underwriter the rights provided for herein.

#### SECTION 9. NON-REDUCTION AND NON-ACCUMULATION OF LIABILITY AND TOTAL LIABILITY

At all times prior to termination hereof this bond shall continue in force for the limit stated in the applicable sections of Item 3 of the Declarations of this bond notwithstanding any previous loss for which the Underwriter may have paid or be liable to pay hereunder; PROVIDED, however, that regardless of the number of years this bond shall continue in force and the number of premiums which shall be payable or paid, the liability of the Underwriter under this bond with respect to all loss resulting from

(a) any one act of burglary, robbery or holdup, or attempt thereat, in which no Partner or Employee is concerned or implicated shall be deemed to be one loss, or

(b) any one unintentional or negligent act on the part of any one person resulting in damage to or destruction or misplacement of Property, shall be

under the terms and conditions of this INVESTMENT COMPANY BLANKET BOND subject to the Limit of Liability hereunder.

deemed to be one loss, or

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(c) all wrongful acts, other than those specified in (a) above, of any one person shall be deemed to be one loss, or

(d) all wrongful acts, other than those specified in (a) above, of one or more persons (which dishonest act(s) or act(s) of Larceny or Embezzlement include, but are not limited to, the failure of an Employee to report such acts of others) whose dishonest act or acts intentionally or unintentionally, knowingly or unknowingly, directly or indirectly, aid or aids in any way, or permits the continuation of, the dishonest act or acts of any other person or persons shall be deemed to be one loss with the act or acts of the persons aided, or

(e) any one casualty or event other than those specified in (a), (b), (c) or (d) preceding, shall be deemed to be one loss, and

shall be limited to the applicable Limit of Liability stated in Item 3 of the Declarations of this bond irrespective of the total amount of such loss or losses and shall not be cumulative in amounts from year to year or from period to period.

Sub-section (c) is not applicable to any situation to which the language of sub-section (d) applies.

#### SECTION 10. LIMIT OF LIABILITY

With respect to any loss set forth in the PROVIDED clause of Section 9 of this bond which is recoverable or recovered in whole or in part under any other bonds or policies issued by the Underwriter to the Insured or to any predecessor in interest of the Insured and terminated or cancelled or allowed to expire and in which the period for discovery has not expired at the time any such loss thereunder is discovered, the total liability of the Underwriter under this bond and under other

bonds or policies shall not exceed, in the aggregate, the amount carried hereunder on such loss or the amount available to the Insured under such other bonds or policies, as limited by the terms and conditions thereof, for any such loss if the latter amount be the larger.

#### SECTION 11. OTHER INSURANCE

If the Insured shall hold, as indemnity against any loss covered hereunder, any valid and enforceable insurance or suretyship, the Underwriter shall be liable hereunder only for such amount of such loss which is in excess of the amount of such other insurance or suretyship, not exceeding, however, the Limit of Liability of this bond applicable to such loss.

#### SECTION 12. DEDUCTIBLE

The Underwriter shall not be liable under any of the Insuring Agreements of this bond on account of loss as specified, respectively, in sub-sections (a), (b), (c), (d) and (e) of Section 9, NON-REDUCTION AND NON-ACCUMULATION OF LIABILITY AND TOTAL LIABILITY, unless the amount of such loss, after deducting the net amount of all reimbursement and/or recovery obtained or made by the Insured, other than from any bond or policy of insurance issued by an insurance company and covering such loss, or by the Underwriter on account thereof prior to payment by the Underwriter of such loss, shall exceed the Deductible Amount set forth in Item 3 of the Declarations hereof (herein called Deductible Amount) and then for such excess only, but in no event for more than the applicable Limit of Liability stated in Item 3 of the Declarations.

The Insured will bear, in addition to the Deductible Amount, premiums on Lost Instrument Bonds as set forth in Section 7.

There shall be no deductible applicable to any loss under Insuring Agreement A sustained by any Investment Company named as Insured herein.

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#### SECTION 13. TERMINATION

The Underwriter may terminate this bond as an entirety by furnishing written notice specifying the termination date which cannot be prior to 60 days after the receipt of such written notice by each Investment Company named as Insured and the Securities and Exchange Commission, Washington, D.C. The Insured may terminate this bond as an entirety by furnishing written notice to the Underwriter. When the Insured cancels, the Insured shall furnish written notice to the Securities and Exchange Commission, Washington, D.C. prior to 60 days before the effective date of the termination. The Underwriter shall notify all other Investment Companies named as Insured of the receipt of such termination notice and the termination cannot be effective prior to 60 days after receipt of written notice by all other Investment Companies. Premiums are earned until the termination date as set forth herein.

This Bond will terminate as to any one Insured immediately upon taking over of such Insured by a receiver or other liquidator or by State or Federal officials, or immediately upon the filing of a petition under any State or Federal statute relative to bankruptcy or reorganization of the Insured, or assignment for the benefit of creditors of the Insured, or immediately upon such Insured ceasing to exist, whether through merger into another entity, or by disposition of all of its assets.

The Underwriter shall refund the unearned premium computed at short rates in accordance with the standard short rate cancellation tables if terminated by the Insured or pro rata if terminated for any other reason.

This Bond shall terminate

(a) as to any Employee as soon as any partner, officer or supervisory Employee of the Insured, who is not in collusion with such Employee, shall learn of any dishonest or fraudulent act(s), including Larceny

or Embezzlement on the part of such Employee without prejudice to the loss of any Property then in transit in the custody of such Employee (See Section 16[d]), or

(b) as to any Employee 60 days after receipt by each Insured and by the Securities and Exchange Commission of a written notice from the Underwriter of its desire to terminate this bond as to such Employee, or

(c) as to any person, who is a partner, officer or employee of any Electronic Data Processor covered under this bond, from and after the time that the Insured or any partner or officer thereof not in collusion with such person shall have knowledge or information that such person has committed any dishonest or fraudulent act(s), including Larceny or Embezzlement in the service of the Insured or otherwise, whether such act be committed before or after the time this bond is effective.

#### SECTION 14. RIGHTS AFTER TERMINATION OR CANCELLATION

At any time prior to the termination or cancellation of this bond as an entirety, whether by the Insured or the Underwriter, the Insured may give to the Underwriter notice that it desires under this bond an additional period of 12 months within which to discover loss sustained by the Insured prior to the effective date of such termination or cancellation and shall pay an additional premium therefor.

Upon receipt of such notice from the Insured, the Underwriter shall give its written consent thereto; provided, however, that such additional period of time shall terminate immediately;

(a) on the effective date of any other insurance obtained by the Insured, its successor in business or any other party, replacing in whole or in part the insurance afforded by this bond, whether or not such other insurance provides coverage for loss sustained prior to its effective date, or

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(b) upon takeover of the Insured's business by any State or Federal official or agency, or by any receiver or liquidator, acting or appointed for this purpose

without the necessity of the Underwriter giving notice of such termination. In the event that such additional period of time is terminated, as provided above, the Underwriter shall refund any unearned premium.

employee of any recognized service company, while such officers, partners, clerks and other employees and employees of service companies perform services for such Corporations in the operation of such systems. For the purpose of the above definition a recognized service company shall be any company providing clerks or other personnel to said Exchanges or Corporation on a contract basis.

The right to purchase such additional period for the discovery of loss may not be exercised by any State or Federal official or agency, or by any receiver or liquidator, acting or appointed to take over the Insured's business for the operation or for the liquidation thereof or for any other purpose.

#### SECTION 15. CENTRAL HANDLING OF SECURITIES

Securities included in the systems for the central handling of securities established and maintained by Depository Trust Company, Midwest Depository Trust Company, Pacific Securities Depository Trust Company, and Philadelphia Depository Trust Company, hereinafter called Corporations, to the extent of the Insured's interest therein as effective by the making of appropriate entries on the books and records of such Corporations shall be deemed to be Property.

The words "Employee" and "Employees" shall be deemed to include the officers, partners, clerks and other employees of the New York Stock Exchange, Boston Stock Exchange, Midwest Stock Exchange, Pacific Stock Exchange and Philadelphia Stock Exchange, hereinafter called Exchanges, and of the above named Corporations, and of any nominee in whose name is registered any security included within the systems for the central handling of securities established and maintained by such Corporations, and any

The Underwriter shall not be liable on account of any loss(es) in connection with the central handling of securities within the systems established and maintained by such Corporations, unless such loss(es) shall be in excess of the amount(s) recoverable or recovered under any bond or policy of insurance indemnifying such Corporations, against such loss(es), and then the Underwriter shall be liable hereunder only for the Insured's share of such excess loss(es), but in no event for more than the Limit of Liability applicable hereunder.

For the purpose of determining the Insured's share of excess loss(es) it shall be deemed that the Insured has an interest in any certificate representing any security included within such systems equivalent to the interest the Insured then has in all certificates representing the same security included within such systems and that such Corporations shall use their best judgement in apportioning the amount(s) recoverable or recovered under any bond or policy of insurance indemnifying such Corporations against such loss(es) in connection with the central handling of securities within such systems among all those having an interest as recorded by appropriate entries in the books and records of such Corporations in Property involved in such loss(es) on the basis that each such interest shall share in the amount(s) so recoverable or recovered in the ratio that the value of each such interest bears to the total value of all such interests and that the Insured's share of such excess loss(es) shall be the amount of the Insured's interest in such Property in excess of the amount(s) so apportioned to the Insured by such Corporations.

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This bond does not afford coverage in favor of such Corporations or Exchanges or any nominee in whose name is registered any security included within the systems for the central handling of securities established and maintained by such Corporations, and upon payment to the Insured by the Underwriter on account of any loss(es) within the systems, an assignment of such of the Insured's rights and causes of action as it may have against such Corporations or Exchanges shall to the extent of such payment, be given by the Insured to the Underwriter, and the Insured shall execute all papers necessary to secure to the Underwriter the rights provided for herein.

#### SECTION 16. ADDITIONAL COMPANIES INCLUDED AS INSURED

If more than one corporation, co-partnership or person or any combination of them be included as

(d) knowledge possessed or discovery made by any partner, officer or supervisory Employee of any Insured shall for the purposes of Section 4 and Section 13 of this bond constitute knowledge or discovery by all the Insured, and

(e) if the first named Insured ceases for any reason to be covered under this bond, then the Insured next named shall thereafter be considered as the first named Insured for the purposes of this bond.

#### SECTION 17. NOTICE AND CHANGE OF CONTROL

Upon the Insured's obtaining knowledge of a transfer of its outstanding voting securities which results in a change in control (as set forth in Section 2(a) (9) of the Investment Company Act of 1940) of the Insured, the Insured shall within thirty (30) days of such knowledge give written notice to the Underwriter setting forth:

the Insured herein:

(a) the total liability of the Underwriter hereunder for loss or losses sustained by any one or more or all of them shall not exceed the limit for which the Underwriter would be liable hereunder if all such loss were sustained by any one of them,

(b) the one first named herein shall be deemed authorized to make, adjust and receive and enforce payment of all claims hereunder and shall be deemed to be the agent of the others for such purposes and for the giving or receiving of any notice required or permitted to be given by the terms hereof, provided that the Underwriter shall furnish each named Investment Company with a copy of the bond and with any amendment thereto, together with a copy of each formal filing of the settlement of each such claim prior to the execution of such settlement,

(c) the Underwriter shall not be responsible for the proper application of any payment made hereunder to said first named Insured,

(a) the names of the transferors and transferees (or the names of the beneficial owners if the voting securities are requested in another name), and

(b) the total number of voting securities owned by the transferors and the transferees (or the beneficial owners), both immediately before and after the transfer, and

(c) the total number of outstanding voting securities.

As used in this section, control means the power to exercise a controlling influence over the management or policies of the Insured.

Failure to give the required notice shall result in termination of coverage of this bond, effective upon the date of stock transfer for any loss in which any transferee is concerned or implicated.

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Such notice is not required to be given in the case of an Insured which is an Investment Company.

#### SECTION 18. CHANGE OR MODIFICATION

This bond or any instrument amending or effecting same may not be changed or modified orally. No changes in or modification thereof shall be effective unless made by written endorsement issued to form a part hereof over the signature of the Underwriter's Authorized Representative. When a bond covers only one Investment Company no change or modification which would adversely affect the rights of the Investment Company shall be effective prior to 60 days after written notification has been furnished to the Securities and Exchange Commission, Washington, D.C. by the Insured or by the Underwriter. If more than one Investment Company is named as the Insured herein, the Underwriter shall give written notice to each Investment Company and to the Securities and Exchange Commission, Washington, D.C. not less than 60 days prior to the effective date of any change or modification which would adversely affect the rights of such Investment Company.

IN WITNESS WHEREOF, the Underwriter has caused this bond to be executed on the Declarations Page.

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ENDORSEMENT #1

This endorsement, effective 12:01 AM July 30, 2008 forms a part of policy number 00-669-12-00 issued to PROSPECT ENERGY CORPORATION LLC

by National Union Fire Insurance Company of Pittsburgh, Pa.

COMPUTER SYSTEMS/VIT

It is agreed that:

1. The attached bond is amended by adding an additional Insuring Agreement as follows:

COMPUTER SYSTEMS

Loss resulting directly from a fraudulent

- (1) entry of data into, or
- (2) change of data elements or programs within a Computer System; provided the fraudulent entry or change causes
  - (a) Property to be transferred, paid or delivered,
  - (b) an account of the Insured, or of its customer, to be added, deleted, debited or credited, or
  - (c) an unauthorized account or a fictitious account to be debited or credited;
- (3) voice instructions or advices having been transmitted to the Insured or its agent(s) by telephone; and provided further, the fraudulent entry or change is made or caused by an individual acting with the manifest intent to:
  - (a) cause the Insured or its agent(s) to sustain a loss, and
  - (b) obtain financial benefit for that individual or for other persons intended by that individual to receive financial benefit,
  - (c) and further provided such voice instructions or advices:

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ENDORSEMENT #1 (Continued)

- (i) were made by a person who purported to represent an individual authorized to make such voice instructions or advices; and
  - (ii) were electronically recorded by the Insured or its agent(s).
- (4) It shall be a condition to recovery under the Computer Systems Rider that the insured or its agent(s) shall to the best of their ability



electronically record all voice instructions or advices received over telephone. The Insured or its agent(s) warrant that they shall make their best efforts to maintain the electronic recording system on a continuous basis. Nothing, however, in this Rider shall bar the Insured from recovery where no recording is available because of mechanical failure of the device used in making such recording, or because of failure of the media used to record a conversation from any cause, or error or omission of any Employee(s) or agent(s) of the Insured.

SCHEDULE OF SYSTEMS

Insureds Proprietary System

2. As used in this Rider, Computer System means
- (a) computers with related peripheral components, including storage components, wherever located,
  - (b) systems and applications software,
  - (c) terminal devices,
  - (d) related communication networks or customer communication systems, and
  - (e) related Electronic Funds Transfer Systems,
- by which data are electronically collected, transmitted, processed, stored, and retrieved,

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ENDORSEMENT #1 (Continued)

3. In addition to the exclusions in the attached bond, the following exclusions are applicable to this Insuring Agreement:
- (a) Loss resulting directly or indirectly from the theft of confidential information, material or data; and
  - (b) Loss resulting directly or indirectly from entries or changes made by an individual authorized to have access to a Computer System who acts in good faith on instructions, unless such instructions are given to that individual by a software contractor (or by a partner, officer or employee thereof) authorized by the Insured to design, develop, prepare, supply service, write or implement programs for the Insured's Computer System.
4. The following portions of the attached bond are not applicable to this Rider:
- (a) the initial paragraph of the bond preceding the Insuring Agreements which reads "... at any time but discovered during the Bond Period,"
5. The coverage afforded by this rider applies only to loss discovered by the Insured during the period this Rider is in force.

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6. All loss or series of losses involving the fraudulent activity of one individual, or involving fraudulent activity in which one individual is implicated, whether or not that individual is specifically identified, shall be treated as one loss. A series of losses involving unidentified individuals but arising from the same method of operation may be deemed by the Underwriter to involve the same individual and in that event shall be treated as one loss.
7. The Limit of Liability for the coverage provided by this Rider shall be One Million Dollars (\$1,000,000).
8. The Underwriter shall be liable hereunder for the amount by which one loss shall be in excess of Ten Thousand Dollars (\$10,000) (herein called the Deductible Amount) but not in excess of the Limit of Liability stated above.

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ENDORSEMENT #1 (Continued)

9. If any loss is covered under this Insuring Agreement and any other Insuring Agreement or Coverage, the maximum amount payable for such loss shall not exceed the largest amount available under anyone Insuring Agreement or Coverage.
10. Coverage under this Rider shall terminate upon termination or cancellation of the bond to which this Rider is attached. Coverage under this rider may also be terminated or cancelled without cancelling the bond as an entirety:
  - (a) 60 days after receipt by the Insured of written notice from the Underwriter of its desire to terminate or cancel coverage under this Rider, or
  - (b) immediately upon receipt by the Underwriter of a written request from the Insured to terminate or cancel coverage under this Rider.

The Underwriter shall refund to the Insured the unearned premium for this coverage under this Rider. The refund shall be computed at short rates if this Rider is terminated or cancelled or reduced by notice from, or at the instance of, the Insured.

	3,014,498	9.5%
David L. Mahoney (20)	22,500	*
Thomas Wiggans (21)	22,500	*
All directors and executive officers as a group (16 persons) (22)	17,417,315	55.2%

\* Less than one percent.

(1) This table is based upon information supplied by officers, directors and principal stockholders. Unless otherwise indicated in the footnotes to this table and subject to community property laws where applicable, Tercica believes that each of the stockholders named in this table has sole voting and investment power with respect to the shares indicated as beneficially owned. Applicable percentages are based on 31,578,517 shares outstanding on April 15, 2005, adjusted as required by rules promulgated by the Securities and Exchange Commission.

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- (2) Includes 5,877,051 shares held by MPM BioVentures III-QP, L.P., 496,634 shares held by MPM BioVentures III GmbH & Co. Beteiligungs KG, 395,146 shares held by MPM BioVentures III, L.P., 116,113 shares held by MPM Asset Management Investors 2002 BVIII LLC and 177,550 shares held by MPM BioVentures III Parallel Fund, L.P. Dr. Henner, one of Tercica's directors, is a general partner at MPM Capital L.P., the management company affiliated with the stockholders listed above, and holds voting and dispositive power for the shares held of record by the stockholders listed above. Dr. Henner disclaims beneficial ownership of these shares, except to the extent of his pecuniary interest therein. The address for MPM Capital L.P. is 111 Huntington Avenue, 31st floor Boston, MA 02199.

- (3) Includes 3,760,784 shares held by Prospect Venture Partners II L.P. and 57,270 shares held by Prospect Associates II, L.P. Dr. Barkas, one of Tercica's directors, is a managing member of Prospect Management Co. II LLC, the management company affiliated with the stockholders listed above, and holds voting and dispositive power for the shares held of record by the stockholders listed above. The address for Prospect Management Co. II, LLC is 435 Tasso Street, Suite 200, Palo Alto, California 94301.
- (4) Consists of 3,000,000 shares held by MedImmune Ventures, Inc., a wholly-owned venture capital subsidiary of MedImmune, Inc., and an option issued to MedImmune Ventures, Inc. to purchase 7,500 shares of common stock, which are fully vested as of April 15, 2005. Wayne T. Hockmeyer is the president of MedImmune Ventures, Inc. and is on an investment committee that holds voting and dispositive power over these shares owned by MedImmune Ventures, Inc. Dr. Hockmeyer resigned from Tercica's Board of Directors effective April 13, 2005. Dr. Hockmeyer disclaims beneficial ownership of these shares. The address for MedImmune, Inc. is One MedImmune Way, Gaithersburg, Maryland 20878.
- (5) Includes 727,594 shares held by Rho Management Trust I, 333,935 shares held by Rho Ventures IV, L.P., 786,168 shares held by Rho Ventures IV (QP), L.P. and 819,301 shares held by Rho Ventures IV GmbH & Co. Beteiligungs KG. These stockholders are affiliated with the management company, Rho Capital Partners, Inc., the management company for Rho Ventures. Mark Leschly, one of Tercica's directors, is a managing member of the general partner of Rho Ventures IV, L.P. and Rho Ventures IV (QP), L.P., a managing director of the general partner of Rho Ventures IV GmbH & Co. Beteiligungs KG and a managing partner of the investment advisor to Rho Management Trust I. Mr. Leschly disclaims beneficial ownership of these shares except to the extent of his pecuniary interest therein. The address of Rho Capital Partners, Inc. is Carnegie Hall Tower, 152 West 57th Street, 23rd Floor, New York, NY 10019.
- (6) Includes 602,352 shares purchased pursuant to early exercised options, of which 176,109 shares are subject to Tercica's right of repurchase within 60 days of April 15, 2005 and options to purchase 150,000 shares of common stock may be exercised pursuant to an early exercise agreement, all of which will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005. Also includes 153,651 shares of common stock held by The John A. Scarlett 1999 Trust U/A dtd November 26, 1999, 15,576 shares of which are subject to Tercica's right of repurchase within 60 days of April 15, 2005, and 154,901 shares of common stock held by The Susan E. Scarlett 1999 Trust U/A dtd November 26, 1999, 15,577 shares of which are subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (7) Includes 556,392 shares held by Boat Harbour Ltd., 1,490 shares acquired through Tercica's 2004 Employee Stock Purchase Plan and options to purchase 112,847 shares of common stock that may be exercised pursuant to early exercise agreements, of which 76,649 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (8) Represents an option to purchase 130,000 shares of common stock that may be exercised pursuant to an early exercise agreement. All of these shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (9) Represents an option to purchase 400,000 shares of common stock that may be exercised pursuant to early exercise agreements. 318,751 of these shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (10) Includes 265,591 shares purchased pursuant to early exercised options, of which 106,759 shares are subject to Tercica's right of repurchase within 60 days of April 15, 2005, 1,511 shares acquired through Tercica's 2004 Employee Stock Purchase Plan and options to purchase 50,000 shares of common stock that may be exercised pursuant to an early exercise agreement, all of which will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (11) Represents an option to purchase 200,000 shares of common stock that may be exercised pursuant to early exercise agreements. All of these shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.

- (12) Represents an option to purchase 110,000 shares of common stock that may be exercised pursuant to an early exercise agreement. All of these shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (13) Includes 1,435 shares acquired through Tercica's 2004 Employee Stock Purchase Plan and options to purchase 150,000 shares of common stock that may be exercised pursuant to early exercise agreements, of which 98,699 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (14) Includes 588 shares acquired through Tercica's 2004 Employee Stock Purchase Plan and options to purchase 125,000 shares of common stock that may be exercised pursuant to early exercise agreements, of which 84,115 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (15) Represents options to purchase 36,250 shares of common stock that may be exercised pursuant to early exercise agreements, of which 22,500 will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005 and the shares described in Note (3) above. Dr. Barkas disclaims beneficial ownership of the shares held by Prospect Management Co. II, LLC, except to the extent of his pecuniary interest therein.
- (16) Represents 10,000 shares purchased pursuant to early exercised options and remaining options to purchase 12,500 shares of common stock that may be exercised pursuant to an early exercise agreement, of which 15,000 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (17) Represents options to purchase 22,500 shares of common stock that may be exercised pursuant to an early exercise agreement, of which 15,000 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005 and the shares described in Note (2) above. Dr. Henner disclaims beneficial ownership of the shares held by MPM Capital L.P., except to the extent of his pecuniary interest therein.
- (18) Includes options to purchase 22,500 shares of common stock that may be exercised pursuant to an early exercise agreement, of which 15,000 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (19) Represents options to purchase 22,500 shares of common stock that may be exercised pursuant to an early exercise agreement, of which 15,000 shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005 and the shares described in Note (5) above. Mark Leschly, one of Tercica's directors, is a managing member of the general partner of Rho Ventures IV, L.P. and Rho Ventures IV (QP), L.P., a managing director of the general partner of Rho Ventures IV GmbH & Co. Beteiligungs KG and a managing partner of the investment advisor to Rho Management Trust I. Mr. Leschly disclaims beneficial ownership of these shares except to the extent of his pecuniary interest therein.
- (20) Represents options to purchase 22,500 shares of common stock that may be exercised pursuant to an early exercise agreement. All of these shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (21) Represents options to purchase 22,500 shares of common stock that may be exercised pursuant to an early exercise agreement. All of these shares will be unvested and subject to Tercica's right of repurchase within 60 days of April 15, 2005.
- (22) Includes 877,943 shares purchased pursuant to early exercised options of which 290,902 shares are subject to Tercica's right of repurchase within 60 days of April 15, 2005, 308,552 shares purchased pursuant to a restricted common stock purchase agreement, 31,153 shares of which are subject to Tercica's right of repurchase within 60 days of April 15, 2005, and options to purchase 1,589,097 shares of common stock, of which 1,343,214 shares are subject to Tercica's right of repurchase if such options are either exercised or early exercised pursuant to option agreements within 60 days of April 15, 2005.

**SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Securities Exchange Act of 1934 (the "1934 Act") requires Tercica's directors and executive officers, and persons who own more than ten percent of a registered class of Tercica's equity securities, to file with the SEC initial reports of ownership and reports of changes in ownership of Tercica's common stock and other equity securities. Officers, directors and greater than ten percent stockholders are required by SEC regulations to furnish us with copies of all Section 16(a) forms they file.

To Tercica's knowledge, based solely on a review of the copies of such reports furnished to us and written representations that no other reports were required, during the fiscal year ended December 31, 2004, all Section 16(a) filing requirements applicable to Tercica's officers, directors and greater than ten percent beneficial owners were complied with; except that one report on Form 4, covering one transaction, was filed late by Thomas Silberg, and one report on Form 4, covering one transaction, was filed late by David Mahoney.

**EQUITY COMPENSATION PLAN INFORMATION**

The following table provides certain information with respect to all of Tercica's equity compensation plans in effect as of December 31, 2004:

<b>Plan Category</b>	<b>Number of securities</b>	<b>Weighted-average exercise price of outstanding options, warrants and rights</b>	<b>Number of securities remaining available for</b>
	<b>to be issued upon exercise of outstanding options, warrants and rights</b>		<b>issuance under equity compensation plans (excluding securities reflected in column (a))</b>
	<b>(a)</b>	<b>(b)</b>	<b>(c)</b>
Equity compensation plans approved by security holders	1,628,875	\$ 5.75	1,597,259(1)
Equity compensation plans not approved by security holders	22,500	\$ 4.00	
<b>Total</b>	<b>1,651,375</b>	<b>\$ 5.72</b>	<b>1,597,259(1)</b>

(1) Of these shares, 71,706 shares remained available for the grant of future rights under Tercica's 2004 Employee Stock Purchase Plan as of December 31, 2004.

All of Tercica's equity compensation plans and arrangements were approved by Tercica's stockholders, with the exception of a single stock option granted to MedImmune Ventures, Inc. to purchase 22,500 shares of common stock at an exercise price of \$4.00 per share, the fair market value of the stock as determined by Tercica's Board of Directors on the date of grant. This stock option provided that it was to vest in three equal installments on each one-year anniversary date of the date of grant until all shares subject to the option are vested in full, subject to the continued status of Dr. Hockmeyer as a director. As of the effective date of Dr. Hockmeyer's resignation from the Board in April 2005, 7,500 shares were vested, and the unvested portion of this stock option expired. This stock option was granted outside of Tercica's stock option plans without the approval of Tercica's security holders.

**EXECUTIVE COMPENSATION**

**Compensation of Directors**

Prior to Tercica's initial public offering in March 2004, Tercica did not pay any cash compensation to its directors, except for Karin Eastham, to whom Tercica paid \$1,875 prior to Tercica's initial public offering. Each non-employee director of Tercica currently receives \$15,000 per year, plus \$2,000 for each meeting attended in

person and \$1,000 for each meeting attended by telephone. Tercica also pays the members, other than the chair, of each committee of the Board an additional \$1,000 per meeting and the chair of each committee an additional \$2,000 per meeting. In the fiscal year ended December 31, 2004, the total compensation paid to non-employee directors was \$173,772. With regard to Dr. Hockmeyer's services, this compensation was paid directly to MedImmune Ventures, Inc. The members of the Board of Directors are also eligible for reimbursement for their expenses incurred in attending Board meetings in accordance with Tercica's policy.

On January 8, 2004, Tercica granted to Dr. Barkas, Tercica's Chairman of the Board, an option to purchase 33,750 shares of common stock, and each of Tercica's other current non-employee directors, other than Dr. Hockmeyer whose option was issued to MedImmune Ventures, Inc., an option to purchase 22,500 shares of common stock. Each of these options vest in three equal installments on each one-year anniversary date of the date of grant until all shares subject to the option are vested in full, subject to the optionee's continued status as a director or, in the case of MedImmune Ventures, Inc.'s grant, the continued status of Dr. Hockmeyer as a director. Each non-employee director of Tercica is also eligible to receive stock option grants under Tercica's 2004 Stock Plan, which became effective on the day prior to the closing of Tercica's initial public offering in March 2004. Under the 2004 Stock Plan, any new non-employee director joining Tercica's Board will automatically receive an option to purchase 22,500 shares of common stock. In addition, non-employee directors, who have been directors for at least six months, will receive a subsequent annual stock option grant to purchase 11,250 shares, or 22,500 shares for a non-employee director who also is the Chairman of the Board, following each annual meeting of Tercica's stockholders, commencing with the 2005 Annual Meeting of Stockholders. All options granted to non-employee directors under the automatic grant provisions of the 2004 Stock Plan have a term of ten years and an exercise price equal to fair market value on the date of grant. Each initial option becomes exercisable as to one-third of the shares subject to the option on each anniversary of the date of grant, provided the non-employee director remains a service provider on such dates. Each annual option grant becomes exercisable as to 100% of the shares subject to the option on the first anniversary of the date of grant, provided the non-employee director remains a service provider on such date. Under the 2004 Stock Plan, in the event of Tercica's change of control, the successor corporation may assume or substitute an equivalent award for each outstanding option. If there is no assumption or substitution of outstanding options, the administrator will provide notice to the recipient that he or she has the right to exercise the option as to all of the shares subject to the award, including shares which would not otherwise be exercisable, for a period of 15 days from the date of the notice. The award will terminate upon the expiration of the 15-day period. Under the 2004 Stock Plan, in the event a non-employee director is terminated on or following a change in control, other than pursuant to a voluntary resignation, his or her options will fully vest and become immediately exercisable.



**Compensation of Executive Officers**

The following table shows for the fiscal years ended December 31, 2002, 2003 and 2004, compensation awarded or paid to, or earned by, Tercica's Chief Executive Officer and its other four most highly compensated executive officers at December 31, 2004 (the "Named Executive Officers"):

**SUMMARY COMPENSATION TABLE**

Name and Principal Position	Year	Annual Compensation			Long-Term Compensation Awards		
		Salary	Bonus*	Other Annual Compensation	Restricted Stock Awards	Securities Underlying Options	All Other Compensation(18)
John A. Scarlett, M.D. (1)	2004	\$ 305,000	\$ 140,000	\$ 56,296(2)			\$ 420
President and Chief Executive Officer	2003	280,000		52,258(3)		87,500	136
	2002	247,085		31,982(4)	(5)	514,852	
	Thomas H. Silberg (6)	2004	218,590	120,000	63,743(7)		300,000
Chief Operating Officer	2003						
	2002						
	Timothy P. Lynch (8)	2004	235,000	60,000	4,011(9)		
Chief Financial Officer and Treasurer	2003	235,000		3,155(10)		87,500	136
	2002	55,436				178,091	
	Ross G. Clark, Ph.D. (11)	2004	225,000	60,000	12,372(12)		
Chief Technical Officer	2003	225,000		17,530(13)		37,500	136
	2002	134,835	21,120	18,775(14)		25,347	
	Michael Parker (15)	2004	225,000	46,000	6,679(16)		
Vice President of Quality	2003	196,010	50,000	21,939(17)		75,000	136
	2002						

(1) In February 2002, Dr. Scarlett joined Tercica as its President and Chief Executive Officer and Dr. Scarlett's annualized salary was \$280,000. Dr. Scarlett's annualized salary was increased to \$330,000 effective July 2004.

(2) Includes \$24,000 related to housing, \$11,395 related to travel incentives, \$20,901 related to health and dental benefits.

(3) Includes \$21,600 related to housing, \$12,676 related to travel incentives, \$17,982 related to health and dental benefits.

(4) Includes \$14,700 related to housing, \$8,883 related to travel incentives, \$6,386 related to health and dental benefits, \$1,210 related to relocation costs and \$803 related to the payment of taxes for such relocation costs.

(5)

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In February 2002, Dr. Scarlett purchased 328,158 shares of common stock at a purchase price of \$0.00625 per share pursuant to his employment agreement. See Employment Contracts, Termination of Employment and Change of Control Arrangements John A. Scarlett, M.D.

- (6) In April 2004, Mr. Silberg joined Tercica as its Chief Operating Officer. Mr. Silberg's annualized salary for 2004 was \$310,000. Mr. Silberg earned a bonus for 2004 of \$70,000 and was paid a signing bonus of \$50,000 in April 2004, which must be returned to Tercica, pro-rata, if Mr. Silberg is not employed by Tercica on October 19, 2005.
- (7) Includes \$63,000 related to housing and \$743 related to health and dental benefits.
- (8) In October 2002, Mr. Lynch joined Tercica as its Chief Financial Officer. Mr. Lynch's annualized salary for 2004 was \$235,000.
- (9) Represents health and dental benefits.

- (10) Includes \$1,000 related to travel incentives and \$2,155 related to health and dental benefits.
- (11) In May 2002, Dr. Clark joined Tercica from Tercica Limited, Tercica's predecessor company in New Zealand, as Tercica's Chief Technical Officer. Dr. Clark's annualized salary for 2004 was \$225,000. In January 2002, Dr. Clark received an additional \$6,471 as salary from Tercica Limited.
- (12) Includes \$5,585 related to travel incentives and \$6,787 related to health and dental benefits.
- (13) Includes \$9,005 related to travel incentives and \$8,525 for health and dental benefits.
- (14) Includes \$15,753 related to housing and \$3,022 related to health and dental benefits.
- (15) In February 2003, Mr. Parker joined Tercica as its Vice President, Quality. Mr. Parker's annualized salary for 2004 was \$225,000. Mr. Parker received a signing bonus of \$50,000 in February 2003, of which \$25,000 must be returned to Tercica if Mr. Parker is not employed by Tercica on February 19, 2005.
- (16) Represents health and dental benefits.
- (17) Includes \$16,000 related to travel incentives and \$5,939 related to health and dental benefits.
- (18) Represents life insurance premiums.
- \* 2004 bonuses were paid in 2005 for 2004 performance.

### Stock Option Grants And Exercises

The following tables show for the fiscal year ended December 31, 2004, certain information regarding options granted to, exercised by, and held at year end by, each of the Named Executive Officers:

#### Option Grants in Last Fiscal Year

Name	Number of Securities Underlying Options Granted	Percent of Total Options Granted to Employees in 2004(2)	Exercise Price Per Share	Expiration Date	Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term(3)	
					5%	10%

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John A. Scarlett, M.D.						
Thomas H. Silberg (1)	300,000	23.4%	\$ 11.19	4/28/2014	\$ 2,111,199	\$ 5,350,193
Timothy P. Lynch						
Ross G. Clark, Ph.D.						
Michael Parker						

- (1) One-fourth of the shares subject to Mr. Silberg's stock option vest one year after the vest date, and 1/48<sup>th</sup> of the remaining shares subject to Mr. Silberg's stock option vest each month thereafter and may be early exercised by Mr. Silberg. The exercise price per share of Mr. Silberg's stock option was equal to the closing price of Tercica's common stock on the grant date. The exercise price may be paid in cash, in shares of Tercica's common stock valued at fair market value on the exercise date or through a cashless exercise procedure involving a same-day sale of the purchased shares.
- (2) The percentage shown under "Percent of Total Options Granted to Employees in 2004" is based on options to purchase an aggregate of 1,282,500 shares granted to Tercica's employees during 2004. This number does not include options to purchase 24,000 shares granted to consultants during 2004.
- (3) The potential realizable value is calculated based on the ten-year term of the option at the time of grant, compounded annually. The potential realizable value is calculated by assuming that the stock price on the date of grant appreciates at the indicated annual rate, compounded annually for the entire term of the option, and that the option is exercised and sold on the last day of its term for the appreciated stock price. Appreciation of 5% and 10% is assumed pursuant to rules promulgated by the SEC and does not represent Tercica's prediction of its stock price performance.

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**Aggregated Option Exercises in Last Fiscal Year and Fiscal Year End Option Values**

Name	Shares Acquired on Exercise	Value Realized	Number of Securities Underlying Unexercised Options at December 31, 2004		Value of Unexercised In-The-Money Options at December 31, 2004(2)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
John A. Scarlett, M.D.					\$	
Thomas H. Silberg (1)			300,000			
Timothy P. Lynch						
Ross G. Clark, Ph.D. (1)			62,847		558,331	
Michael Parker (1)			75,000		705,000	

- (1) Stock option grants named in the table above may be exercised pursuant to an early exercise agreement.
- (2) Amounts presented under the caption Value of Unexercised In-The-Money Options at December 31, 2004 are based on the closing price per share of Tercica's common stock as of December 31, 2004 of \$10.00 per share, less the exercise price payable for such shares, multiplied by the number of shares subject to the stock option, without taking into account any taxes that might be payable in connection with the transaction.

**Employment Contracts, Termination of Employment and Change of Control Arrangements**
***John A. Scarlett, M.D.***

In February 2002, Tercica entered into an employment agreement that was amended in May 2002 and February 2005, and a restricted common stock purchase agreement for the purchase of 328,158 shares of common stock, with John A. Scarlett, Tercica's President and Chief Executive Officer. Pursuant to the agreement, Dr. Scarlett purchased 328,158 shares of common stock at a price of \$0.00625 per share. Of the 328,158 shares of common stock purchased in February 2002, 186,904 shares were initially subject to vesting and a right of repurchase in favor of Tercica. On February 27, 2003, 46,726 shares were released from Tercica's right of repurchase. With respect to the shares purchased in February 2002, Tercica's right of repurchase lapses at the rate of 3,893 shares each month. In addition, pursuant to the amendment to Dr. Scarlett's employment agreement, in June 2002, Dr. Scarlett was granted an option to purchase 514,852 shares of Tercica's common stock, representing 5.078% of the total outstanding equity shares calculated on a fully diluted basis after taking into account the issuance of Tercica's Series A preferred stock on the date of grant. Dr. Scarlett purchased these shares pursuant to a restricted stock purchase agreement in December 2002. With respect to the shares purchased in December 2002, Tercica's right of repurchase lapsed as to 25% of the shares in May 2003 and lapses at the rate of 10,726 shares each month thereafter.

All of the shares of common stock purchased under Dr. Scarlett's February 2002 restricted common stock purchase agreement and 25% of the shares purchased under his December 2002 restricted common stock purchase agreement, will immediately vest in the event Dr. Scarlett is terminated without cause or terminates his own employment for good reason, as these terms are defined in his employment agreement. In the event Dr. Scarlett is terminated without cause or terminates his own employment for good reason prior to a change of control or is terminated on or after 12 months following a change of control, he will be entitled to 12 months salary, 12 months accelerated vesting on all of his options and equity grants, as well as reimbursement of all health care premiums for 12 months and Tercica's right to repurchase shares of common stock purchased by Dr. Scarlett pursuant to the February 2002 restricted stock purchase agreement will lapse. In the event Dr. Scarlett is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to 24 months salary, fully accelerated vesting on all of his options and equity grants, as well as reimbursement of all health care premiums for 18 months, and Tercica's right to repurchase shares of common stock purchased by Dr. Scarlett will lapse.

*Thomas H. Silberg*

In April 2004, Tercica entered into an employment agreement that was amended in February 2005 with Thomas H. Silberg, Tercica's Chief Operating Officer, pursuant to which Mr. Silberg was granted an option to

purchase 300,000 shares of Tercica's common stock. These shares will vest 25% upon the one-year anniversary date of the date of grant and continue to vest at a rate of 6,250 shares a month thereafter. In the event Mr. Silberg is terminated without cause or terminates his own employment for good reason within 12 months after a change of control, he will be entitled to severance pay equal to 12 months salary and the vesting for all of the unvested stock option shares will be accelerated so as to vest as of the date of termination. In the event Mr. Silberg is terminated without cause at any time not within 12 months following a change of control, he will be entitled to a severance pay equal to six months salary. Mr. Silberg was provided a signing bonus of \$50,000, which must be returned on a pro rata basis if he voluntarily resigns or is terminated for cause within 18 months after his start date. In addition, Tercica agreed to reimburse Mr. Silberg up to \$25,000 for usual and customary moving expenses incurred in relocating to the San Francisco Bay Area. If Mr. Silberg voluntarily resigns or is terminated for cause within two years after his relocation to the San Francisco Bay Area, the reimbursement must be returned on a pro rata basis. Tercica also agreed to reimburse Mr. Silberg up to \$75,000 for usual and customary costs associated with the sale of his house and/or the purchase of a home in the San Francisco Bay Area. If Mr. Silberg voluntarily resigns or is terminated with cause within two years of his start date, the reimbursement must be returned on a pro rata basis.

***Timothy P. Lynch***

In September 2002, Tercica entered into an employment agreement that was amended in February 2005 with Timothy P. Lynch, Tercica's Chief Financial Officer and Treasurer, pursuant to which Mr. Lynch was granted an option to purchase 178,091 shares of common stock under Tercica's 2002 Executive Stock Plan. Mr. Lynch purchased these shares pursuant to a restricted stock purchase agreement in December 2002. Tercica's right of repurchase with respect to 25% of the shares lapsed in October 2003 and continues to lapse at the rate of 3,710 shares each month thereafter. In the event Mr. Lynch is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to severance pay equal to 24 months salary and full accelerated vesting for all his options, and Tercica's repurchase right will lapse as to all of the shares then subject to Tercica's repurchase right. In the event that Mr. Lynch is terminated without cause at any time not within 12 months of a change of control, he will be entitled to six months salary.

***Ross G. Clark, Ph.D.***

In May 2002, Tercica entered into an employment agreement that was amended in February 2005 with Ross G. Clark, Tercica's Chief Technical Officer, pursuant to which Dr. Clark was granted an option to purchase 25,347 shares of Tercica's common stock, representing 0.25% of Tercica's total outstanding equity shares calculated on a fully diluted basis after taking into account the issuance of Tercica's Series A preferred stock on the date of grant. These shares vested 25% upon the one-year anniversary date of the date of grant and continue to vest at a rate of shares a month thereafter. Under the employment agreement, in the event Dr. Clark is terminated without cause or terminates his own employment for good reason prior to a change of control, as these terms are defined in the agreement, or is terminated on or after 12 months following a change of control, he will be entitled to 12 months salary and 12 months accelerated vesting on all of his options and equity grants, as well as reimbursement of all health care premiums for 12 months. In the event Dr. Clark is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to 12 months salary and accelerated vesting on all of his options and equity grants, as well as reimbursement of all health care premiums for 18 months.

***Michael Parker***

In December 2002, Tercica entered into an employment agreement that was amended in February 2005 with Michael Parker, Tercica's Vice President, Quality, pursuant to which Mr. Parker was granted an option to purchase 62,500 shares of Tercica's common stock. These shares vested 25% upon the one-year anniversary date of the date of grant and continue to vest at a rate of 1,302 shares a month thereafter. In the event Mr. Parker is terminated without cause or terminates his own employment for good reason within 12 months following a





change of control, he will be entitled to severance pay equal to six months salary and Tercica's repurchase right will lapse as to 50% of the shares then subject to Tercica's repurchase right. In the event that Mr. Parker is terminated without cause at any time not within 12 months of a change of control, he will be entitled to three months salary. In addition, Tercica agreed to provide Mr. Parker a signing bonus of \$50,000, of which \$25,000 must be returned to Tercica if Mr. Parker is not employed by Tercica on February 19, 2005.

***Chris Rivera***

In April 2005, Tercica entered into an employment agreement with Chris Rivera, Tercica's Senior Vice President, Commercial Operations, pursuant to which Mr. Rivera was granted an option to purchase 130,000 shares of Tercica's common stock. These shares will vest 25% upon the one-year anniversary date of the date of grant and continue to vest at a rate of 2,708 shares a month thereafter. In the event Mr. Rivera is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to severance pay equal to six months salary and Tercica's repurchase right will lapse as to 50% of the shares then subject to Tercica's repurchase right. In the event that Mr. Rivera is terminated without cause at any time not within 12 months of a change of control, he will be entitled to three months salary.

***Stephen N. Rosenfield***

In June 2004, Tercica entered into an employment agreement, that was amended in February 2005, with Stephen N. Rosenfield, Tercica's Senior Vice President of Legal Affairs, General Counsel and Secretary. Mr. Rosenfield was granted an option to purchase 180,000 shares of Tercica's common stock. These shares will vest 25% upon the one-year anniversary date of the date of grant and continue to vest at a rate of 3,750 shares a month thereafter. In the event Mr. Rosenfield is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to severance pay equal to 12 months salary and all of the unvested stock option shares will be accelerated so as to vest as of the date of termination. In the event that Mr. Rosenfield is terminated without cause at any time not within 12 months of a change in control, he will be entitled to six months salary.

***Thorsten von Stein, Ph.D.***

In December 2004, Tercica entered into an employment agreement with Thorsten von Stein, Ph.D., Tercica's Chief Medical Officer. Dr. von Stein was granted an option to purchase 110,000 shares of Tercica's common stock. In the event Dr. von Stein is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to severance pay equal to six months salary and 50% of the unvested stock option shares will be accelerated so as to vest as of the date of termination. In the event that Dr. von Stein is terminated without cause at any time not within 12 months of a change in control, he will be entitled to six months salary.

***Andrew Grethlein***

In March 2003, Tercica entered into an employment agreement with Andrew Grethlein, Tercica's Vice President, Manufacturing. Dr. Grethlein was granted an option to purchase 87,500 shares of Tercica's common stock. These shares vested 25% upon the one-year anniversary date of the date of grant and continue to vest at a rate of 1,823 shares a month thereafter. In the event Dr. Grethlein is terminated without cause or terminates his own employment for good reason within 12 months following a change of control, he will be entitled to severance pay equal to six months salary and 50% of the unvested stock option shares will be accelerated so as to vest as of the date of termination. In the event that Dr. Grethlein is terminated without cause at any time not within 12 months of a change in control, he will be entitled to three months salary.



**Certain Relationships and Related Transactions****Stock Sales**

Since January 1, 2004, the following executive officers, directors and 5% or more stockholders have purchased shares of common stock either from Tercica or in connection with Tercica's underwritten public offerings in the amounts and as of the dates set forth below:

	<u>Number of Shares</u>	<u>Purchase Price</u>	<u>Date of Purchase</u>
<b>5% Stockholders:</b>			
MPM Capital L.P. (1)	370,001	\$ 3,330,009.00	03/17/04
Prospect Management Co. II, LLC (2)	555,555	4,999,995.00	03/17/04
MedImmune, Inc. (3)	2,000,000	16,000,000.00	02/11/05
Rho Ventures (4)	667,000	6,003,000.00	03/17/04
Rho Ventures (4)	325,000	2,600,000.00	02/11/05
<b>Directors and Executive Officers:</b>			
Ross G. Clark, Ph.D.	490	3,748.50	05/17/04
	1,000	7,650.00	11/15/04
Timothy P. Lynch	511	3,909.15	05/17/04
	1,000	7,650.00	11/15/04
Andrew Grethlein, Ph.D.	435	3,327.75	05/17/04
	1,000	7,650.00	11/15/04
Michael Parker	147	1,124.55	05/17/04
	441	3,373.65	11/15/04
Karin Eastham	10,000	40,000.00	01/28/04

- (1) Includes shares held by entities affiliated with MPM Capital L.P. Dr. Henner, one of Tercica's directors, is a general partner at MPM Capital L.P.
- (2) Includes shares held by entities affiliated with Prospect Management Co. II, LLC. Dr. Barkas, one of Tercica's directors, is a managing member of Prospect Management Co. II, LLC.
- (3) Consists of shares held by MedImmune Ventures, Inc., a wholly owned venture capital subsidiary of MedImmune, Inc. Wayne T. Hockmeyer, one of Tercica's former directors, is the president of MedImmune Ventures, Inc.
- (4) Includes shares held by entities affiliated with Rho Capital Partners, Inc. Mr. Leschly, one of Tercica's directors, is a managing partner at Rho Capital Partners, Inc., the management company for Rho Ventures.

**Investor Rights Agreement**

Tercica, the prior holders of Tercica's preferred stock and Drs. Scarlett, Clark and Isaksson have entered into an agreement pursuant to which these stockholders will be entitled to require Tercica to register their shares under the Securities Act, subject to limitations and restrictions, on two occasions. Also, if at anytime Tercica proposes to register any of its securities under the Securities Act of 1933, as amended, either for Tercica's account or for the account of other securities holders, the holders of these shares will be entitled to notice of the registration and will be entitled to include, at Tercica's expense, their shares of Tercica's common stock in the registration. In addition, these stockholders may require Tercica, at Tercica's expense and on not more than two occasions in any 12-month period, to file a registration statement on Form S-3 under the

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Securities Act of 1933, as amended, covering their shares of Tercica's common stock when registration of Tercica's shares under this form becomes possible. These rights terminate on the earlier of five years after the effective date of Tercica's initial offering public offering in March 2004, or, with respect to an individual stockholder, when such holder is able to sell all his shares pursuant to Rule 144 under the Securities Act in any 90-day period. These registration rights are subject to conditions and limitations, including the right of underwriters to limit the number of shares of Tercica's common stock included in the registration statement.

***Employment Agreements***

Tercica has entered into employment agreements with each of its executive officers. For more information regarding these agreements, see Employment Contracts, Termination of Employment and Change of Control Arrangements.

***Director and Officer Indemnification***

Tercica's restated certificate of incorporation contains provisions limiting the liability of Tercica's directors. Tercica's bylaws provide that Tercica must indemnify its directors and officers and may indemnify Tercica's other employees and agents to the fullest extent permitted by the Delaware General Corporation Law. Tercica's bylaws also permit Tercica to secure insurance on behalf of any officer, director, employee or other agent for any liability arising out of his or her actions in that capacity, regardless of whether Tercica's bylaws would otherwise permit indemnification. Tercica has entered and expects to continue to enter into agreements to indemnify its directors, executive officers and other employees as determined by the Board of Directors. These agreements provide for indemnification for related expenses including attorneys' fees, judgments, fines and settlement amounts incurred by any of these individuals in any action or proceeding. Tercica believes that these bylaw provisions and indemnification agreements are necessary to attract and retain qualified persons as directors and officers. Tercica also maintains directors' and officers' liability insurance.

**Compensation Committee Interlocks and Insider Participation**

During 2004, Tercica's Compensation Committee was comprised of Dr. Henner, Mr. Leschly and Dr. Hockmeyer, who resigned from Tercica's Board of Directors in April 2005. As noted above, Tercica's Compensation Committee is currently comprised of Dr. Henner, Mr. Leschly and Mr. Wiggans. No member of the Compensation Committee is or was formerly an officer or employee of Tercica. None of Tercica's executive officers serves as a member of the board of directors or compensation committee of any entity that has one or more executive officers who serve on Tercica's Board or Compensation Committee.

**REPORT OF THE COMPENSATION COMMITTEE OF THE BOARD OF DIRECTORS ON EXECUTIVE COMPENSATION(1)**

**To: The Board of Directors**

The Compensation Committee oversees Tercica's overall compensation program for its employees and executive officers. In addition, the Committee evaluates the performance and recommends the compensation of the Chief Executive Officer to the Board of Directors. The Committee is comprised entirely of independent directors who are not officers or employees of Tercica.

**Compensation Philosophy**

During 2004, Tercica's compensation program was designed to:

reward employees for Tercica's overall performance and for individual performance with respect to goals, responsibilities and adherence to company values;

attract and retain individuals who are capable of leading Tercica in achieving its business objectives in an industry characterized by competitiveness, growth and a challenging business environment; and

provide substantial alignment of management's interests with the long-term interests of stockholders.

The Committee believes that Tercica's compensation program is consistent with the Committee's policy of maximizing stockholder value over time.

**Compensation Survey**

In 2004, the Committee engaged the services of an independent compensation and benefits consulting company in order to conduct a survey and review of Tercica's salary, bonus, stock incentive award and benefits history for executive officers, compared to a group of biotechnology and pharmaceutical companies of a size and complexity similar to that of Tercica. Based on the analysis, the consultant concluded that the levels of executive compensation provided during 2004 were generally competitive with the levels offered by the comparator companies surveyed, although in individual cases, certain individuals were above and certain individuals were below competitive norms.

**Factors Affecting the Evaluation of Executive Performance**

Executive officers are evaluated with respect to their achievement of their individual goals and responsibilities, adherence to Tercica's values and the achievement of the annual company-wide goals set by the Board of Directors. For 2004, Tercica's successful initial public offering ( IPO ) in March 2004 and progress made toward the filing Tercica's new drug application ( NDA ) were assigned significant weight. Future compensation

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for executive officers will continue to be based in large part on Tercica's ability to effectively develop and implement strategies and performance that enable Tercica to achieve its company-wide goals and enhance stockholder value.

### **Executive Officer Salaries**

Salaries for executive officers are based principally on the Committee's evaluation of individual job performance, an assessment of the salaries paid by similar companies to executive officers holding equivalent

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- (1) The material in this report is not soliciting material, is not deemed filed with the SEC and is not to be incorporated by reference into any filing of Tercica under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date hereof and irrespective of any general incorporation language in any such filing.

positions, and, with respect to executive officers other than the Chief Executive Officer, recommendations made by the Chief Executive Officer. In setting salaries, the Committee neither bases its considerations on any single factor nor does it specifically assign relative weights to factors, but rather considers a mix of factors and evaluates individual performance against that mix both in absolute terms and in relation to other company executives. The 2004 salaries of the Named Executive Officers are shown in the "Salary" column of the Summary Compensation Table.

### **Executive Officer Bonuses**

The Committee sets the annual compensation pool for bonuses for all employees, which is contingent upon performance against individual goals and responsibilities and against annual company-wide goals set by the Board of Directors. Executive bonuses in 2004 were primarily based on performance against individual goals and responsibilities, adherence to Tercica's values and an assessment of the executive's contribution to the achievement of Tercica's 2004 goals, which included the successful completion of the IPO in March 2004 and progress toward the filing of Tercica's NDA. The bonuses awarded to the Named Executive Officers for 2004 are shown in the "Bonus" column of the Summary Compensation Table, as is the signing bonus paid to Mr. Silberg in 2004.

### **Executive Officer Long-Term Incentive Compensation**

Long-term incentive awards, such as stock options, are designed to ensure that incentive compensation is linked to the long-term performance of Tercica's common stock. Tercica has provided long-term compensation to certain members of senior management under Tercica's 2004 Stock Plan. The plan provides Tercica with the ability to periodically reward key employees, including executive officers, with options to purchase shares of Tercica's common stock as well as other stock purchase rights. The size of the option grant is generally intended to reflect the executive officer's position with Tercica and his or her individual job performance and contributions to Tercica's annual goals. An executive officer's equity ownership position in Tercica is also considered in determining the size of the option grant. The value of stock options is tied to the future performance of Tercica's common stock and provides value to the recipient only when the price of Tercica's common stock increases above the option grant price. Through option grants and other stock awards, executives receive significant equity incentives to build long-term stockholder value.

In 2004, no stock options were granted to the Named Executive Officers listed in the Summary Compensation Table, except for an option granted to Mr. Silberg for the purchase of 300,000 shares of Tercica's common stock under Tercica's 2004 Stock Plan, which was granted in connection with his joining Tercica in April 2004.

Additional long-term equity incentives are provided through Tercica's 2004 Employee Stock Purchase Plan in which all eligible employees, including eligible executive officers of Tercica, may purchase stock of Tercica, subject to specified limits, at 85% of fair market value.

### **Compensation of the Chief Executive Officer**

The Committee recommended Dr. Scarlett's 2004 salary to the Board of Directors. In setting Dr. Scarlett's base salary for 2004, the Committee and Board of Directors evaluated the same factors for establishing the salary levels of the executive officers generally, as well as Tercica's 2004 financial and operating performance, and the performance of Tercica's common stock. In addition, the Committee and Board of Directors considered the status of Dr. Scarlett as Tercica's most senior officer, a review of the compensation for chief executive officers of comparable companies, and the important role he performed in achieving overall corporate goals. No particular weighting was assigned to any factor, although the Committee and the Board of Directors weighted Tercica's successful IPO in March 2004 and progress made toward filing of the NDA more heavily.





The Board of Directors had set Dr. Scarlett's base salary of \$280,000, which continued into January 2004, and raised it to \$330,000 effective July 1, 2004. In 2004, Tercica did not award any equity-based compensation to Dr. Scarlett because of his significant current levels of stock ownership. The bonus award recommended by the Committee for 2004 and set by the Board of Directors was \$140,000, based primarily on the factors set forth above. Dr. Scarlett did not receive separate compensation for serving as a member of the Board of Directors.

#### **Federal Tax Considerations**

Section 162(m) of the Internal Revenue Code of 1986, as amended (the Code) limits Tercica to a deduction for federal income tax purposes of no more than \$1 million of compensation paid to certain executive officers in a taxable year. Compensation above \$1 million may be deducted if it is performance-based compensation within the meaning of the Code.

Section 162(m) and applicable Treasury regulations offer a number of transitional exceptions to this deduction limit for pre-existing compensation plans, arrangements and binding contracts adopted prior to the time a company becomes publicly held. As a result, the Committee believes that at the present time it is quite unlikely that the compensation paid to any executive officer in a taxable year that is subject to the deduction limit will exceed \$1 million. Therefore, the Committee has not yet established a policy for determining which forms of incentive compensation awarded to Tercica's executive officers shall be designed to qualify as performance-based compensation. The Committee intends to continue to evaluate the effects of the statute and any applicable Treasury regulations and to comply with Code section 162(m) in the future to the extent consistent with Tercica's best interests.

THE COMPENSATION COMMITTEE

OF THE BOARD OF DIRECTORS

Dennis Henner (Chairman)

Mark Leschly

Thomas Wiggans

**PERFORMANCE MEASUREMENT COMPARISON(1)**

The following graph shows the total stockholder return of an investment of \$100 in cash on March 17, 2004, the date Tercica's common stock first started trading on the Nasdaq National Market, for: (i) Tercica's common stock, (ii) the Nasdaq Stock Market (U.S.) Index; and (iii) the Nasdaq Biotechnology Index. Pursuant to applicable SEC rules, all values are to assume reinvestment of the full amount of all dividends; however, no dividends have been declared on Tercica's common stock to date. The stockholder return shown on the graph below is not necessarily indicative of future performance, and Tercica does not make or endorse any predictions as to future stockholder returns.

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### HOUSEHOLDING OF PROXY MATERIALS

The SEC has adopted rules that permit companies and intermediaries (e.g., brokers) to satisfy the delivery requirements for proxy statements and annual reports with respect to two or more stockholders sharing the same address by delivering a single proxy statement addressed to those stockholders. This process, which is commonly referred to as householding, potentially means extra convenience for stockholders and cost savings for companies.

This year, a number of brokers with account holders who are Tercica stockholders will be householding Tercica's proxy materials. A single proxy statement may be delivered to multiple stockholders sharing an address unless contrary instructions have been received from the affected stockholders. Once you have received notice from your broker that it will be householding communications to your address, householding will continue until you are notified otherwise or until you notify your broker or Tercica that you no longer wish to participate in householding. If, at any time, you no longer wish to participate in householding and would prefer to receive a separate proxy statement and annual report in the future you may (1) notify your broker, (2) direct your written request to: Investor Relations, Tercica Inc., 651 Gateway Boulevard, Suite 950, South San Francisco, California 94080 (after July 10, 2005, please direct your written request to: Investor Relations, Tercica Inc., 2000 Sierra Point Parkway, Brisbane, California 94005) or (3) contact Tercica's Investor Relations department at (650) 624-4977. Stockholders who currently receive multiple copies of the proxy statement at their address and would like to request householding of their communications should contact their broker. In addition, Tercica will promptly deliver, upon written or oral request to the address or telephone number above, a separate copy of the annual report and proxy statement to a stockholder at a shared address to which a single copy of the documents was delivered.

**OTHER MATTERS**

The Board of Directors knows of no other matters that will be presented for consideration at the Annual Meeting. If any other matters are properly brought before the meeting, it is the intention of the persons named in the accompanying proxy to vote on such matters in accordance with their best judgment.

By Order of the Board of Directors

/s/ Stephen N. Rosenfield

**Stephen N. Rosenfield**

Secretary

April 29, 2005

**A copy of Tercica's Annual Report to the Securities and Exchange Commission on Form 10-K for the fiscal year ended December 31, 2004 is available without charge upon written request to: Investor Relations, Tercica, Inc., 651 Gateway Boulevard, Suite 950, South San Francisco, California 94080. After July 10, 2005, please direct your written request to: Investor Relations, Tercica, Inc., 2000 Sierra Point Parkway, Brisbane, California 94005.**

**TERCICA, INC.**

**CHARTER OF THE AUDIT COMMITTEE  
OF THE BOARD OF DIRECTORS**

**PURPOSES:**

The purposes of the Audit Committee of the Board of Directors (the Board) of Tercica, Inc. (the Company) are to:

Monitor (i) the accounting and financial reporting processes of the Company, including the Company's internal accounting and financial controls, (ii) the integrity of the Company's financial statements, and (iii) the Company's compliance with legal and regulatory requirements as they relate to financial statements or accounting matters;

Retain and oversee the independent auditors of the Company's financial statements; and

Provide the Board with the results of its monitoring and recommendations derived therefrom, as well as such additional information and materials as it may deem necessary to make the Board aware of significant financial matters that require the Board's attention.

In addition, the Audit Committee will undertake those specific duties and responsibilities listed below and such other duties as the Board may from time to time prescribe.

**MEMBERSHIP:**

The Audit Committee members will be appointed by, and will serve at the discretion of, the Board. The Audit Committee will consist of at least three members of the Board. Members of the Audit Committee must meet the following criteria:

Each member will be an independent director, as defined in (i) NASD Marketplace Rule 4200(a)(15) and (ii) Rule 10A-3(b)(i) under the Securities Exchange Act of 1934, as amended; provided, that one non-employee director who is not independent under NASD Marketplace Rule 4200(a)(15) may serve on the Audit Committee if the Board has made the required determination under NASD Marketplace Rule 4350(d)(2)(B);

Each member will be able to read and understand fundamental financial statements, in accordance with NASD Marketplace Rule 4350(d)(2)(A)(iv); and

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At least one member will qualify as a financial expert under NASD Marketplace Rule 4350(d)(2) and under Item 401(h) of Regulation S-K.

The Board will annually appoint the members of the Audit Committee and the Chair of the Audit Committee, immediately following the Company's annual meeting of stockholders.

### **RESPONSIBILITIES:**

The responsibilities of the Audit Committee will include the following:

Reviewing management's report on its assessment of the effectiveness of the Company's internal control over financial reporting as of the end of the most recent fiscal year and the independent auditors' report on management's assessment;

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Reviewing before release the disclosure regarding the Company's system of internal controls required to be contained in the Company's periodic filings, and reviewing the attestations or reports by the auditors relating to such disclosure;

Appointing, compensating, retaining and overseeing the work of the auditors (including resolving disagreements between management and the auditors regarding financial reporting) for the purpose of issuing an audit report or performing other audit, review or attest services or related work;

Pre-approving (or designating a member to pre-approve) audit and non-audit services provided to the Company by the auditors and other public accounting firms (or subsequently approving non-audit services when subsequent approval is necessary and permissible);

Reviewing and providing guidance with respect to the external audit and the Company's relationship with its auditors, including (i) reviewing the auditors' qualifications, performance and independence, (ii) reviewing the auditor's proposed audit scope and audit approach, (iii) discussing with the auditors the financial statements and audit findings, including any matters described in Statement of Accounting Standards (SAS) No. 61, and (iv) reviewing reports submitted to the Audit Committee by the auditors in accordance with the applicable requirements of the Securities and Exchange Commission (the SEC);

Reviewing and discussing with management and the auditors the annual audited financial statements and quarterly unaudited financial statements, including the Company's disclosures under Management's Discussion and Analysis of Financial Condition and Results of Operations, prior to filing the Company's Annual Report on Form 10-K and Quarterly Reports on Form 10-Q with the SEC;

Directing the auditors to review before filing with the SEC the Company's interim financial statements included in Quarterly Reports on Form 10-Q, using professional standards and procedures for conducting such reviews;

Reviewing (or designating a member to review) before release the unaudited quarterly operating results in the Company's quarterly earnings release;

Reviewing with management and the auditors (i) the Company's significant accounting policies, (ii) the impact of changes in accounting policies and other financial reporting developments, whether voluntary or pursuant to regulatory or accounting initiatives, including the effect of alternative GAAP methods on the Company's financial statements, (iii) any transactions as to which management obtained SAS No. 50 letters, (iv) the impact of off-balance sheet structures on the Company's financial statements, and (v) any auditing or accounting issues concerning the Company's employee benefit plans;

Reviewing with management and the auditors any correspondence with or findings by regulatory agencies, and any employee complaints or published reports that raise material issues, regarding the Company's financial statements or accounting policies;

Reviewing, in conjunction with counsel, any legal matters that could have a significant impact on the Company's financial statements;

Reviewing the Company's policies regarding conflicts of interest, reviewing past or proposed transactions between the Company, members of the Board and management for such conflicts, and reviewing and approving in advance any proposed related party transactions;

Reviewing the Company's risk management policies, including its investment policies and performance for cash and short-term investments;



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Instituting special investigations relating to financial statements or accounting policies with full access to all books, records, facilities and personnel of the Company;

Retaining and obtaining advice and assistance from outside legal, accounting or other advisors;

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Establishing and maintaining free and open means of communication between the Audit Committee, the auditors and management;

Establishing procedures for receiving, retaining and treating complaints received by the Company regarding accounting, internal accounting controls or auditing matters and procedures for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters;

Reviewing its own charter (including its structure, processes and membership requirements) at least annually;

Providing a report in the Company's proxy statement as required by the rules and regulations of the SEC; and

Determining the appropriate funding for payment of compensation (i) to the auditors for the purpose of rendering or issuing an audit report or performing other audit, review or attest services and (ii) to any legal, accounting or other advisors employed by the Audit Committee.

While the Audit Committee has the responsibilities and powers set forth in this Charter, it is not the duty of the Audit Committee to plan or conduct audits or to determine that the Company's financial statements and disclosures are complete and accurate and are in accordance with GAAP and applicable rules and regulations.

**MEETINGS:**

The Audit Committee will meet as often as it determines, but not less frequently than once quarterly.

The Audit Committee, in its discretion, will ask members of management or others to attend its meetings (or portions thereof) and to provide pertinent information as necessary. The Audit Committee will meet separately with the Chief Executive Officer and separately with the Chief Financial Officer of the Company at such times as are appropriate to review the financial affairs of the Company. The Audit Committee will meet periodically in separate executive session with the auditors as well as any internal auditors/financial controllers of the Company, at such times as it deems appropriate to fulfill the responsibilities of the Audit Committee under this charter.

**MINUTES:**

The Audit Committee will maintain written minutes of its meetings, which minutes will be filed with the minutes of the meetings of the Board.

**REPORTS:**

In addition to preparing the report in the Company's proxy statement in accordance with the rules and regulations of the SEC, the Audit Committee will summarize its reviews, findings and recommendations to the Board as may be appropriate, consistent with the Audit Committee's charter.

**COMPENSATION:**

Members of the Audit Committee shall receive such fees for their service as Audit Committee members as may be determined by the Board in its sole discretion. Such fees may include retainers or per meeting fees. Fees may be paid in such form of consideration as is determined by the Board.

Members of the Audit Committee may not receive any compensation from the Company except the fees that they receive for service as members of the Board or any committee thereof.

**DELEGATION OF AUTHORITY:**

The Audit Committee may delegate to one or more designated members of the Audit Committee the authority to pre-approve audit and permissible non-audit services, provided such pre-approval decision is presented to the full Audit Committee at its scheduled meetings.

**TERCICA, INC.**

**CHARTER OF THE CORPORATE GOVERNANCE AND NOMINATING COMMITTEE  
OF THE BOARD OF DIRECTORS**

(Amended November 23, 2004)

**PURPOSES:**

The Corporate Governance and Nominating Committee ( CGC ) of the Board of Directors (the Board ) of Tercica, Inc. (the Company ) will monitor the composition of the Board and, when appropriate, seek, screen and recommend for nomination qualified candidates for election to the Board at the Company s Annual Meeting of Stockholders. In addition, the CGC will seek qualified candidates to fill vacancies on the Board subject to appointment by the Board. The CGC will evaluate candidates identified on its own initiative as well as candidates referred to it by other members of the Board, by the Company s management, by stockholders who submit names to the Company s Secretary for referral to the CGC, or by other external sources. The CGC will also evaluate the Board s structure and practices and, when appropriate, recommend new policies to the full Board.

**NOMINATION/APPOINTMENT POLICY:**

The Board believes that it is in the best interests of the Company and its stockholders to obtain highly qualified candidates to the Board. The CGC will seek for nomination and appointment candidates with excellent decision-making ability, business experience, relevant expertise, personal integrity and reputation.

**MEMBERSHIP:**

The CGC will consist of a minimum of three members of the Board, each of whom shall be an independent director within the meaning of Rule 4200 of the Manual of the National Association of Securities Dealers, Inc. The members of the CGC will be appointed by and serve at the discretion of the Board.

**RESPONSIBILITIES:**

The responsibilities of the CGC shall include the following:

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Reviewing Board structure, composition, and practices, and making recommendations on these matters to the Board;

Reviewing, soliciting and making recommendations to the Board and stockholders of the Company with respect to candidates for election to the Board;

Overseeing compliance by the Company's chief executive officer and senior financial officers with the Code of Ethics for Principal Executive and Senior Financial Officers, as adopted by the Company;

Overseeing compliance by the Company's employees with Code of Business Conduct and Ethics, as adopted by the Company;

Establishing procedures for receiving, retaining and treating complaints received by the Company regarding its practices (except with respect to accounting, internal accounting controls or auditing matters, which such matters shall be forwarded to the Audit Committee) and procedures for the confidential, anonymous submission by employees of concerns regarding questionable practices (except with respect to accounting or auditing matters, which such matters shall be forwarded to the Audit Committee);

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Overseeing and monitoring the Company's compliance with legal and regulatory requirements, except as compliance relates to financial statements or accounting matters (which is the duty of the Audit Committee);

Reviewing management's monitoring of compliance with the Company's standards of business contact and with the Foreign Corrupt Practices Act;

Reviewing with management and the independent auditor any correspondence with regulators or governmental agencies and any employee complaints or published reports that raise material issues with respect to all matters other than with respect to the Company's financial statements or accounting policies (which is the duty of the Audit Committee);

Reviewing the findings of any examination by regulatory agencies other than with respect to the Company's financial statements or accounting policies (which is the duty of the Audit Committee);

If necessary, instituting special investigations with full access to all books, records, facilities and personnel of the Company, other than with respect to financial statements or accounting policies (which is the duty of the Audit Committee); and

Performing such other tasks as may be delegated to it from time to time by the Board.

**MEETINGS:**

Meetings of the CGC will be held at the pleasure of the Board and the members of the CGC, from time to time, in response to needs of the Board.

**MINUTES:**

The CGC will maintain written minutes of its meetings, which minutes will be filed with the minutes of the meetings of the Board.

**REPORTS:**

The CGC will summarize its examinations and recommendations to the Board as may be appropriate, consistent with the CGC's charter.

**COMPENSATION:**

Members of the CGC shall receive such fees for their service as CGC members as may be determined by the Board in its sole discretion. Such fees may include retainers or per meeting fees. Fees may be paid in such form of consideration as is determined by the Board.









