NORTHFIELD LABORATORIES INC /DE/
Form 10-Q
April 10, 2006

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

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED FEBRUARY 28, 2006

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE TRANSITION PERIOD FROM _______________ TO _______________

COMMISSION FILE NUMBER 0-24050

NORTHFIELD LABORATORIES INC.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| DELAWARE<br>(State or other jurisdiction of incorporation or organization) | 36-3378733<br>(I.R.S. Employer Identification Number) |
| 1560 SHERMAN AVENUE, SUITE 1000, EVANSTON, ILLINOIS<br>(Address of principal executive offices) | 60201-4800<br>(Zip Code) |

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (847) 864-3500

INDICATE BY CHECK MARK WHETHER THE REGISTRANT (1) HAS FILED ALL REPORTS REQUIRED TO BE FILED BY SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 DURING THE PRECEDING 12 MONTHS (OR FOR SUCH SHORTER PERIOD THAT THE REGISTRANT WAS REQUIRED TO FILE SUCH REPORTS), AND (2) HAS BEEN SUBJECT TO SUCH FILING REQUIREMENTS FOR THE PAST 90 DAYS.

YES X NO ___

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A LARGE ACCELERATED FILER, AN ACCELERATED FILER, OR A NON-ACCELERATED FILER. SEE DEFINITION OF "ACCELERATED FILER OR LARGE ACCELERATED FILER" IN RULE 12B-2 OF THE EXCHANGE ACT. (CHECK ONE):

LARGE ACCELERATED FILER ___ ACCELERATED FILER X NON-ACCELERATED FILER ___

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A SHELL COMPANY (AS DEFINED IN RULE 12B-2 OF THE EXCHANGE ACT). YES ___ NO X

AS OF FEBRUARY 28, 2006, REGISTRANT HAD 26,772,938 SHARES OF COMMON STOCK OUTSTANDING

================================================================================

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This Quarterly Report contains forward-looking statements concerning, among other things, our prospects, clinical and regulatory developments affecting our potential product and our business strategies. These forward-looking statements are identified by the use of such terms as "intends," "expects," "plans," "estimates," "anticipates," "forecasts," "should," "believes" and similar terms.

These forward-looking statements involve risks and uncertainties. Actual results may differ materially from those predicted by the forward-looking statements because of various factors and possible events, including those discussed under "Risk Factors" in our Annual Report on Form 10-K filed with the Securities and Exchange Commission and those matters discussed under "Legal Proceedings" in this Quarterly Report. Because these forward-looking statements involve risks and uncertainties, actual results may differ significantly from those predicted in these forward-looking statements. You should not place undue weight on these statements. These statements speak only as of the date of this document or, in the case of any document incorporated by reference, the date of that document.

All subsequent written and oral forward-looking statements attributable to Northfield or any person acting on our behalf are qualified by the cautionary statements in this section and in our Annual Report. We will have no obligation to revise these forward-looking statements.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
Northfield Laboratories Inc.:

We have reviewed the balance sheet of Northfield Laboratories Inc. (a company in the development stage) as of February 28, 2006, and the related statements of operations for the three-month periods ended February 28, 2006 and 2005, and the statements of operations and cash flows for the nine-month periods ended February 28, 2006 and 2005, and for the period from June 19, 1985 (inception) through February 28, 2006. We have also reviewed the statements of shareholders' equity (deficit) for the nine-month period ended February 28, 2006 and for the period from June 19, 1985 (inception) through February 28, 2006. These financial statements are the responsibility of the Company's management.

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

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

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheet of Northfield Laboratories Inc. as of May 31, 2005, and the related statements of operations, shareholders' equity (deficit), and cash flows for the year then ended and for the period from June 19, 1985 (inception) through May 31, 2005 (not presented herein); and in our report dated August 12, 2005, we expressed an unqualified opinion on those financial statements. In our opinion, the information set forth in the accompanying balance sheet as of May 31, 2005 and in the accompanying statements of operations, cash flows and shareholders' equity (deficit) is fairly stated, in all material respects, in relation to the statements from which it has been derived.

/s/ KPMG LLP

Chicago, Illinois
April 7, 2006

NORTHFIELD LABORATORIES INC.
(a company in the development stage)

Balance Sheets

February 28, 2006 and May 31, 2005

| | FEBRUARY 28, 2006 | MAY 31, 2005 |
|---|---|---|
| | (unaudited) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 49,502,733 | 6,800,405 |
| Marketable securities | 30,810,081 | 91,330,289 |
| Prepaid expenses | 281,087 | 826,741 |
| Other current assets | -- | 139,808 |
| Total current assets | 80,593,901 | 99,097,243 |
| Property, plant, and equipment | 15,281,206 | 14,796,631 |
| Accumulated depreciation | (14,165,914) | (13,961,694) |
| Net property, plant, and equipment | 1,115,292 | 834,937 |
| Other assets | 69,064 | 69,392 |
| | $ 81,778,257 | 100,001,572 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $ 3,196,617 | 3,325,570 |
| Accrued expenses | 80,559 | 110,679 |
| Accrued compensation and benefits | 619,944 | 539,783 |
| Total current liabilities | 3,897,120 | 3,976,032 |
| Other liabilities | 239,240 | 251,582 |

| | | |
|---|---|---|
| Total liabilities | 4,136,360 | 4,227,614 |
| Shareholders' equity: | | |
| Preferred stock, $.01 par value. Authorized 5,000,000 shares; none issued and outstanding | -- | -- |
| Common stock, $.01 par value. Authorized 60,000,000 shares; issued 26,774,655 at February 28, 2006 and 26,752,739 at May 31, 2005 | 267,747 | 267,527 |
| Additional paid-in capital | 241,223,371 | 240,997,444 |
| Deficit accumulated during the development stage | (163,805,807) | (145,361,011) |
| Deferred compensation | (18,021) | (104,609) |
| | 77,667,290 | 95,799,351 |
| Less cost of 1,717 common shares in treasury | (25,393) | (25,393) |
| Total shareholders' equity | 77,641,897 | 95,773,958 |
| | $ 81,778,257 | 100,001,572 |

See accompanying notes to financial statements and accountants' review report.

NORTHFIELD LABORATORIES INC.

(a company in the development stage)

Statements of Operations

Three and nine months ended February 28, 2006 and February 28, 2005 and for the period from June 19, 1985 (inception) through February 28, 2006

| | THREE MONTHS ENDED FEBRUARY 28, | | NINE MONTHS ENDED |
|---|---|---|---|
| | 2006 | 2005 | 2006 |
| | (unaudited) | (unaudited) | (unaudited) |
| Revenues - license income | $ -- | -- | -- |
| Costs and expenses: | | | |
| Research and development | 5,786,424 | 3,817,764 | 16,453,600 |
| General and administrative | 1,453,876 | 1,310,923 | 4,302,696 |
| | 7,240,300 | 5,128,687 | 20,756,296 |
| Other income and expense: | | | |
| Interest income | 845,342 | 281,109 | 2,311,500 |
| Interest expense | -- | -- | -- |
| | $ 845,342 | 281,109 | 2,311,500 |
| Net loss before cumulative effect of change in accounting principle | (6,394,958) | (4,847,578) | (18,444,796) |
| Cumulative effect of change in accounting principle | -- | -- | -- |

| | | | |
|---|---|---|---|
| Net loss | $(6,394,958) | (4,847,578) | (18,444,796) |
| Net loss per share - basic and diluted | $ (0.24) | (0.21) | (0.69) |
| Shares used in calculation of per share data - basic and diluted | 26,769,380 | 22,658,213 | 26,764,146 |

See accompanying notes to financial statements and accountants' review report.

NORTHFIELD LABORATORIES INC.
(a company in the development stage)

Statements of Shareholders' Equity (Deficit)

Nine months ended February 28, 2006 and for the period
from June 19, 1985 (inception) through February 28, 2006

| | PREFERRED STOCK | | COMMON STOCK | |
|---|---|---|---|---|
| | NUMBER OF SHARES | AGGREGATE AMOUNT | NUMBER OF SHARES | AGGREGATE AMOUNT |
| Issuance of common stock on August 27, 1985 | -- | $-- | 3,500,000 | $ 35,000 |
| Issuance of Series A convertible preferred stock at $4.00 per share on August 27, 1985 (net of costs of issuance of $79,150) | -- | -- | -- | -- |
| Net loss | -- | -- | -- | -- |
| Balance at May 31, 1986 | -- | -- | 3,500,000 | 35,000 |
| Net loss | -- | -- | -- | -- |
| Deferred compensation relating to grant of stock options | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1987 | -- | -- | 3,500,000 | 35,000 |
| Issuance of Series B convertible preferred stock at $35.68 per share on August 14, 1987 (net of costs of issuance of $75,450) | -- | -- | -- | -- |
| Net loss | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1988 | -- | -- | 3,500,000 | 35,000 |
| Issuance of common stock at $24.21 per share on June 7, 1988 (net of costs of issuance of $246,000) | -- | -- | 413,020 | 4,130 |
| Conversion of Series A convertible preferred stock to common stock on June 7, 1988 | -- | -- | 1,250,000 | 12,500 |
| Conversion of Series B convertible preferred stock to common stock on June 7, 1988 | -- | -- | 1,003,165 | 10,032 |
| Exercise of stock options at $2.00 per share | -- | -- | 47,115 | 471 |
| Issuance of common stock at $28.49 per share on March 6, 1989 (net of costs of issuance of $21,395) | -- | -- | 175,525 | 1,755 |
| Issuance of common stock at $28.49 per share on March 30, 1989 (net of costs of | | | | |

| | | | | |
|---|---|---|---|---|
| issuance of $10,697) | -- | -- | 87,760 | 878 |
| Sale of options at $28.29 per share to purchase common stock at $.20 per share on March 30, 1989 (net of costs of issuance of $4,162) | -- | -- | -- | -- |
| Net loss | -- | -- | -- | -- |
| Deferred compensation relating to grant of stock options | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1989 | -- | -- | 6,476,585 | 64,766 |
| Net loss | -- | -- | -- | -- |
| Deferred compensation relating to grant of stock options | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1990 | -- | -- | 6,476,585 | 64,766 |
| Net loss | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1991 | -- | -- | 6,476,585 | 64,766 |
| Exercise of stock warrants at $5.60 per share | -- | -- | 90,000 | 900 |
| Net loss | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1992 | -- | -- | 6,566,585 | 65,666 |
| Exercise of stock warrants at $7.14 per share | -- | -- | 15,000 | 150 |
| Issuance of common stock at $15.19 per share on April 19, 1993 (net of costs of issuance of $20,724) | -- | -- | 374,370 | 3,744 |
| Net loss | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1993 | -- | -- | 6,955,955 | 69,560 |
| Net loss | -- | -- | -- | -- |
| Issuance of common stock at $6.50 per share on May 26, 1994 (net of costs of issuance of $2,061,149) | -- | -- | 2,500,000 | 25,000 |
| Cancellation of stock options | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1994 | -- | -- | 9,455,955 | 94,560 |
| Net loss | -- | -- | -- | -- |
| Issuance of common stock at $6.50 per share on June 20, 1994 (net of issuance costs of $172,500) | -- | -- | 375,000 | 3,750 |
| Exercise of stock options at $7.14 per share | -- | -- | 10,000 | 100 |
| Exercise of stock options at $2.00 per share | -- | -- | 187,570 | 1,875 |
| Cancellation of stock options | -- | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- | -- |
| Balance at May 31, 1995 | -- | $-- | 10,028,525 | $100,285 |

See accompanying notes to financial statements and accountants' review report.

| SERIES A CONVERTIBLE PREFERRED STOCK | SERIES B CONVERTIBLE PREFERRED STOCK | DEFICIT ACCUMULATED |
|---|---|---|

| NUMBER OF SHARES | AGGREGATE AMOUNT | NUMBER OF SHARES | AGGREGATE AMOUNT | ADDITIONAL PAID-IN CAPITAL | DURING THE DEVELOPMENT STAGE | DEFERRED COMPEN- SATION | TREASURY SHARES | H (D |
|---|---|---|---|---|---|---|---|---|
| -- | $ -- | -- | $ -- | $ (28,000) | $ -- | $ -- | -- | $ |
| 250,000 | 250,000 | -- | -- | 670,850 | -- | -- | -- | |
| -- | -- | -- | -- | -- | (607,688) | -- | -- | |
| 250,000 | 250,000 | -- | -- | 642,850 | (607,688) | -- | -- | |
| -- | -- | -- | -- | -- | (2,429,953) | -- | -- | (2 |
| -- | -- | -- | -- | 2,340,000 | -- | (2,340,000) | -- | |
| -- | -- | -- | -- | -- | -- | 720,000 | -- | |
| 250,000 | 250,000 | -- | -- | 2,982,850 | (3,037,641) | (1,620,000) | -- | (1 |
| -- | -- | 200,633 | 200,633 | 6,882,502 | -- | -- | -- | 7 |
| -- | -- | -- | -- | -- | (3,057,254) | -- | -- | (3 |
| -- | -- | -- | -- | -- | -- | 566,136 | -- | |
| 250,000 | 250,000 | 200,633 | 200,633 | 9,865,352 | (6,094,895) | (1,053,864) | -- | 3 |
| -- | -- | -- | -- | 9,749,870 | -- | -- | -- | 9 |
| (250,000) | (250,000) | -- | -- | 237,500 | -- | -- | -- | |
| -- | -- | (200,633) | (200,633) | 190,601 | -- | -- | -- | |
| -- | -- | -- | -- | 93,759 | -- | -- | -- | |
| -- | -- | -- | -- | 4,976,855 | -- | -- | -- | 4 |
| -- | -- | -- | -- | 2,488,356 | -- | -- | -- | 2 |
| -- | -- | -- | -- | 7,443,118 | -- | -- | -- | 7 |
| -- | -- | -- | -- | -- | (791,206) | -- | -- | |
| -- | -- | -- | -- | 683,040 | -- | (683,040) | -- | |
| -- | -- | -- | -- | -- | -- | 800,729 | -- | |
| -- | -- | -- | -- | 35,728,451 | (6,886,101) | (936,175) | -- | 27 |
| -- | -- | -- | -- | -- | (3,490,394) | -- | -- | (3 |
| -- | -- | -- | -- | 699,163 | -- | (699,163) | -- | |
| -- | -- | -- | -- | -- | -- | 546,278 | -- | |
| -- | -- | -- | -- | 36,427,614 | (10,376,495) | (1,089,060) | -- | 25 |
| -- | -- | -- | -- | -- | (5,579,872) | -- | -- | (5 |
| -- | -- | -- | -- | -- | -- | 435,296 | -- | |
| -- | -- | -- | -- | 36,427,614 | (15,956,367) | (653,764) | -- | 19 |
| -- | -- | -- | -- | 503,100 | -- | -- | -- | |
| -- | -- | -- | -- | -- | (7,006,495) | -- | -- | (7 |
| -- | -- | -- | -- | -- | -- | 254,025 | -- | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| -- | -- | -- | -- | 36,930,714 | (22,962,862) | (399,739) | -- | 13 |
| -- | -- | -- | -- | 106,890 | -- | -- | -- | |
| -- | -- | -- | -- | 5,663,710 | -- | -- | -- | 5 |
| -- | -- | -- | -- | -- | (8,066,609) | -- | -- | (8 |
| -- | -- | -- | -- | -- | -- | 254,025 | -- | |
| -- | -- | -- | -- | 42,701,314 | (31,029,471) | (145,714) | -- | 11 |
| -- | -- | -- | -- | -- | (7,363,810) | -- | -- | (7 |
| -- | -- | -- | -- | 14,163,851 | -- | -- | -- | 14 |
| -- | -- | -- | -- | (85,400) | -- | 85,400 | -- | |
| -- | -- | -- | -- | -- | -- | 267 | -- | |
| -- | -- | -- | -- | 56,779,765 | (38,393,281) | (60,047) | -- | 18 |
| -- | -- | -- | -- | -- | (7,439,013) | -- | -- | (7 |
| -- | -- | -- | -- | 2,261,250 | -- | -- | -- | 2 |
| -- | -- | -- | -- | 71,300 | -- | -- | -- | |
| -- | -- | -- | -- | 373,264 | -- | -- | -- | |
| -- | -- | -- | -- | (106,750) | -- | 106,750 | -- | |
| -- | -- | -- | -- | -- | -- | (67,892) | -- | |
| -- | $ -- | -- | $ -- | $59,378,829 | $(45,832,294) | $ (21,189) | -- | $13 |

NORTHFIELD LABORATORIES INC.
(a company in the development stage)

Statements of Shareholders' Equity (Deficit)

Nine months ended February 28, 2006 and for the period
from June 19, 1985 (inception) through February 28, 2006

| | PREFERRED STOCK | | COMMON |
|---|---|---|---|
| | NUMBER OF SHARES | AGGREGATE AMOUNT | NUMBER OF SHARES |
| Net loss | -- | $-- | -- |
| Issuance of common stock at $17.75 per share on August 9, 1995 (net of issuance costs of $3,565,125) | -- | -- | 2,925,000 |
| Issuance of common stock at $17.75 per share on September 11, 1995 (net of issuance costs of $423,238) | -- | -- | 438,750 |
| Exercise of stock options at $2.00 per share | -- | -- | 182,380 |
| Exercise of stock options at $6.38 per share | -- | -- | 1,500 |
| Exercise of stock options at $7.14 per share | -- | -- | 10,000 |
| Cancellation of stock options | -- | -- | -- |
| Amortization of deferred compensation | -- | -- | -- |
| Balance at May 31, 1996 | -- | -- | 13,586,155 |
| Net loss | -- | -- | -- |

| | | | |
|---|---|---|---|
| Exercise of stock options at $0.20 per share | -- | -- | 263,285 |
| Exercise of stock options at $2.00 per share | -- | -- | 232,935 |
| Exercise of stock options at $7.14 per share | -- | -- | 10,000 |
| Amortization of deferred compensation | -- | -- | -- |
| Balance at May 31, 1997 | -- | -- | 14,092,375 |
| Net loss | -- | -- | -- |
| Exercise of stock options at $7.14 per share | -- | -- | 5,000 |
| Amortization of deferred compensation | -- | -- | -- |
| Balance at May 31, 1998 | -- | -- | 14,097,375 |
| Net loss | -- | -- | -- |
| Non-cash compensation | -- | -- | -- |
| Exercise of stock options at $7.14 per share | -- | -- | 17,500 |
| Exercise of stock warrants at $8.00 per share | -- | -- | 125,000 |
| Balance at May 31, 1999 | -- | -- | 14,239,875 |
| Net loss | -- | -- | -- |
| Non-cash compensation | -- | -- | -- |
| Exercise of stock options at $13.38 per share | -- | -- | 2,500 |
| Balance at May 31, 2000 | -- | -- | 14,242,375 |
| Net loss | -- | -- | -- |
| Non-cash compensation | -- | -- | -- |
| Exercise of stock options at $6.38 per share | -- | -- | 6,000 |
| Exercise of stock options at $10.81 per share | -- | -- | 17,500 |
| Balance at May 31, 2001 | -- | -- | 14,265,875 |
| Net loss | -- | -- | -- |
| Balance at May 31, 2002 | -- | -- | 14,265,875 |
| Net loss | -- | -- | -- |
| Balance at May 31, 2003 | -- | -- | 14,265,875 |
| Issuance of common stock at $5.60 per share on July 28, 2003 (net of costs of issuance of $909,229) | -- | -- | 1,892,857 |
| Issuance of common stock to directors at $6.08 per share on October 30, 2003 | -- | -- | 12,335 |
| Deferred compensation related to stock grants | -- | -- | 25,500 |
| Amortization of deferred compensation | -- | -- | -- |
| Issuance of common stock at $5.80 per share on January 29, 2004 (net of costs of issuance of $1,126,104) | -- | -- | 2,585,965 |
| Issuance of common stock at $5.80 per share on February 18, 2004 (net of costs of issuance of $116,423) | -- | -- | 237,008 |
| Issuance of common stock at $5.80 per share on April 15, 2004 (net of costs of issuance of $192,242) | -- | -- | 409,483 |
| Issuance of common stock at $12.00 per share on May 18, 2004 (net of costs of issuance of $1,716,831.36) | -- | -- | 1,954,416 |
| Exercise of stock options at $6.38 per share | -- | -- | 15,000 |
| Net loss | -- | -- | -- |
| Balance at May 31, 2004 | | | 21,398,439 |
| Deferred compensation related to stock grants | -- | -- | 5,500 |
| Amortization of deferred compensation | -- | -- | -- |
| Exercise of stock options between $5.08 and $14.17 per share | -- | -- | 167,875 |
| Cost of shares in treasury, 1,717 shares | -- | -- | -- |
| Issuance of common stock to directors at $12.66 per share on September 21, 2004 | -- | -- | 5,925 |
| Issuance of common stock at $15.00 per share on February 9, 2005 (net of costs of issuance of $4,995,689) | -- | -- | 5,175,000 |
| Net loss | -- | -- | -- |

| | | | |
|---|---|---|---|
| Balance at May 31, 2005 | | $ | 26,752,739 |
| Amortization of deferred compensation (unaudited) | -- | -- | -- |
| Exercise of stock options at $7.13 and $10.66 per share (unaudited) | -- | -- | 2,875 |
| Issuance of common stock to directors at $13.05 per share on September 29, 2005 (unaudited) | -- | -- | 5,750 |
| Issuance of common stock to directors at $13.21 per share on October 3, 2005 (unaudited) | -- | -- | 1,135 |
| Issuance of common stock to director at $10.67 per share on February 24, 2006 (unaudited) | | | 1,406 |
| Exercise of stock options at $10.66, $5.15 and $11.09 per share (unaudited) | | | 8,000 |
| Exercise of stock options at $10.66 and $ 7.13 per share (unaudited) | | | 2,750 |
| Net loss (unaudited) | -- | -- | -- |
| Balance at February 28, 2006 (unaudited) | | $ | 26,774,655 |

See accompanying notes to financial statements and accountants' review report.

| SERIES A CONVERTIBLE PREFERRED STOCK | | SERIES B CONVERTIBLE PREFERRED STOCK | | | DEFICIT | | |
|---|---|---|---|---|---|---|---|
| NUMBER OF SHARES | AGGREGATE AMOUNT | NUMBER OF SHARES | AGGREGATE AMOUNT | ADDITIONAL PAID-IN CAPITAL | ACCUMULATED DURING THE DEVELOPMENT STAGE | DEFERRED COMPEN- SATION | TREASU SHARE |
| -- | $-- | -- | $-- | $ -- | $ (4,778,875) | $ -- | - |
| -- | -- | -- | -- | 48,324,374 | -- | -- | - |
| -- | -- | -- | -- | 7,360,187 | -- | -- | - |
| -- | -- | -- | -- | 362,937 | -- | -- | - |
| -- | -- | -- | -- | 9,555 | -- | -- | - |
| -- | -- | -- | -- | 71,300 | -- | -- | - |
| -- | -- | -- | -- | (80,062) | -- | 80,062 | - |
| -- | -- | -- | -- | -- | -- | (62,726) | - |
| -- | -- | -- | -- | 115,427,120 | (50,611,169) | (3,853) | - |
| -- | -- | -- | -- | -- | (4,245,693) | -- | - |
| -- | -- | -- | -- | 50,025 | -- | -- | - |
| -- | -- | -- | -- | 463,540 | -- | -- | - |
| -- | -- | -- | -- | 71,300 | -- | -- | - |
| -- | -- | -- | -- | -- | -- | 2,569 | - |
| -- | -- | -- | -- | 116,011,985 | (54,856,862) | (1,284) | - |
| -- | -- | -- | -- | -- | (5,883,378) | -- | - |
| -- | -- | -- | -- | 35,650 | -- | -- | - |
| -- | -- | -- | -- | -- | -- | 1,284 | - |
| -- | -- | -- | -- | 116,047,635 | (60,740,240) | -- | - |
| -- | -- | -- | -- | -- | (7,416,333) | -- | - |
| -- | | -- | -- | 14,354 | -- | -- | - |
| -- | -- | -- | -- | 124,775 | -- | -- | - |
| -- | -- | -- | -- | 998,750 | -- | -- | - |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| -- | -- | -- | -- | 117,185,514 | (68,156,573) | -- | - |
| -- | -- | -- | -- | -- | (9,167,070) | -- | - |
| -- | -- | -- | -- | 57,112 | -- | -- | - |
| -- | -- | -- | -- | 33,425 | -- | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | -- | -- | -- | 117,276,051 | (77,323,643) | -- | - |
| -- | -- | -- | -- | -- | (10,174,609) | -- | - |
| -- | -- | -- | -- | -- | -- | -- | - |
| -- | -- | -- | -- | 38,220 | -- | -- | - |
| -- | -- | -- | -- | 189,000 | -- | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | -- | -- | -- | 117,503,271 | (87,498,252) | -- | - |
| -- | -- | -- | -- | -- | (10,717,360) | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | -- | -- | -- | 117,503,271 | (98,215,612) | -- | - |
| -- | -- | -- | -- | -- | (12,250,145) | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | -- | -- | -- | 117,503,271 | (110,465,757) | -- | - |
| -- | -- | -- | -- | 9,671,843 | -- | -- | - |
| -- | -- | -- | -- | 74,877 | -- | -- | - |
| -- | -- | -- | -- | 190,995 | -- | (191,250) | - |
| -- | -- | -- | -- | -- | -- | 35,630 | - |
| -- | -- | -- | -- | 13,846,633 | -- | -- | - |
| -- | -- | -- | -- | 1,255,853 | -- | -- | - |
| -- | -- | -- | -- | 2,178,664 | -- | -- | - |
| -- | -- | -- | -- | 21,716,616 | -- | -- | - |
| -- | -- | -- | -- | 95,550 | -- | -- | - |
| -- | -- | -- | -- | -- | (14,573,798) | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | -- | -- | -- | 166,534,302 | (125,039,555) | (155,620) | - |
| -- | -- | -- | -- | 71,055 | -- | (71,110) | - |
| -- | -- | -- | -- | -- | -- | 122,121 | - |
| -- | -- | -- | -- | 1,739,585 | -- | -- | - |
| -- | -- | -- | -- | -- | -- | -- | (25,39 |
| -- | -- | -- | -- | 74,941 | -- | -- | - |
| -- | -- | -- | -- | 72,577,561 | -- | -- | - |
| -- | -- | -- | -- | -- | (20,321,456) | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | $-- | -- | $-- | $240,997,444 | $(145,361,011) | $(104,609) | (25,39 |
| -- | -- | -- | -- | -- | -- | 86,588 | - |
| -- | -- | -- | -- | 29,295 | -- | -- | - |
| -- | -- | -- | -- | 74,943 | -- | -- | - |
| -- | -- | -- | -- | 14,988 | -- | -- | - |
| | | | | 14,986 | | | |
| | | | | 65,075 | | | |
| | | | | 26,640 | | | |
| -- | -- | -- | -- | -- | (18,444,796) | -- | - |
| --- | --- | --- | --- | ------------ | ------------- | --------- | ------ |
| -- | $-- | -- | $-- | $241,223,371 | $(163,805,807) | $ (18,021) | (25,39 |
| === | === | === | === | =========== | ============ | ======== | ====== |

NORTHFIELD LABORATORIES INC.
(a company in the development stage)

Statements of Cash Flows

Nine months ended February 28, 2006 and 2005
and for the period from June 19, 1985
(inception) through February 28, 2006

| | NINE MONTHS ENDED FEBRUARY 28, | | CU |
|---|---|---|---|
| | 2006 | 2005 | FE |
| | (unaudited) | (unaudited) | |
| Cash flows from operating activities: | | | |
| Net loss | $(18,444,796) | (14,646,246) | |
| Adjustments to reconcile net loss to net cash used in operating activities: | | | |
| Marketable security amortization | (1,301,084) | 0 | |
| Depreciation and amortization | 204,220 | 470,605 | |
| Non-cash compensation | 191,588 | 164,055 | |
| Loss on sale of equipment | -- | -- | |
| Changes in assets and liabilities: | | | |
| Prepaid expenses | 545,654 | 261,268 | |
| Other current assets | 139,808 | (79,389) | |
| Other assets | 328 | -- | |
| Accounts payable | (128,953) | (388,792) | |
| Accrued expenses | (30,120) | (65,116) | |
| Accrued compensation and benefits | 80,161 | (52,954) | |
| Other liabilities | (12,342) | (1,101) | |
| Net cash used in operating activities | (18,755,536) | (14,337,670) | |
| Cash flows from investing activities: | | | |
| Purchase of property, plant, equipment, and capitalized engineering costs | (484,575) | (201,582) | |
| Proceeds from sale of land and equipment | -- | -- | |
| Proceeds from matured marketable securities | 146,794,000 | 11,225,000 | |
| Proceeds from sale of marketable securities | -- | -- | |
| Purchase of marketable securities | (84,972,708) | (95,769,935) | |
| Net cash provided by (used in) investing activities | 61,336,717 | (84,746,517) | |
| Cash flows from financing activities: | | | |
| Proceeds from issuance of common stock | 121,147 | 79,327,988 | |
| Payment of common stock issuance costs | -- | (4,995,689) | |
| Proceeds from issuance of preferred stock | -- | -- | |
| Proceeds from sale of stock options to purchase common shares | -- | -- | |
| Proceeds from issuance of notes payable | -- | -- | |
| Repayment of notes payable | -- | -- | |

| | | |
|---|---|---|
| Net cash provided by financing activities | 121,147 | 74,332,299 |
| Net increase (decrease) in cash | 42,702,328 | (24,751,888) |
| Cash at beginning of period | 6,800,405 | 39,042,884 |
| Cash at end of period | $ 49,502,733 | 14,290,996 |
| Supplemental schedule of noncash financing activities: | | |
| Exercise of stock option, 5,000 shares in exchange for 1,717 treasury shares. | $ -- | -- |

See accompanying notes to financial statements and accountants' review report.

NORTHFIELD LABORATORIES INC.
(A COMPANY IN THE DEVELOPMENT STAGE)
NOTES TO FINANCIAL STATEMENTS
FEBRUARY 28, 2006
(UNAUDITED)

(1) BASIS OF PRESENTATION

The interim financial statements presented are unaudited but, in the opinion of management, have been prepared in conformity with accounting principles generally accepted in the United States of America applied on a basis consistent with those of the annual financial statements. Such interim financial statements reflect all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods presented. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the full fiscal years. The interim financial statements should be read in connection with the audited financial statements for the year ended May 31, 2005.

(2) USE OF ESTIMATES

Our management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from those estimates.

(3) COMPUTATION OF NET LOSS PER SHARE

Basic earnings per share is based on the weighted average number of shares outstanding and excludes the dilutive effect of unexercised common stock equivalents. Diluted earnings per share is based on the weighted average number of shares outstanding and includes the dilutive effect of unexercised common stock equivalents. Because we reported net losses for all periods presented, basic and diluted per share amounts are the same. As of February 28, 2006, we have 1,758,375 options and 212,392 warrants that were excluded from the net loss per share calculation because their inclusion would have been anti-dilutive.

(4) STOCK OPTIONS

We account for our fixed plan stock options under the intrinsic value method of accounting prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations in accounting for options granted to directors, officers, and key employees under the plans. As such, compensation expense is recorded on the date of grant and amortized over the period of service only if the current market value of the underlying stock exceeded the exercise price. No stock option based employee compensation cost is reflected in net loss, as each option granted under these plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

The following table illustrates the effect on net loss if we had applied the fair value recognition provisions of Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock Based Compensation" to the measurement of stock-based employee compensation,

including a straight-line recognition of compensation costs over the related vesting periods for fixed awards:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | February 28, 2006 | February 28, 2005 | February 28, 2006 | February 28, 2005 |
| | (unaudited) | (unaudited) | (unaudited) | (unaudited) |
| Net loss as reported | $(6,394,958) | (4,847,578) | (18,444,796) | (14,646,246) |
| Add: Stock based compensation expense included in statements of operations | 35,818 | 32,346 | 191,588 | 164,055 |
| Deduct: Total stock based compensation expense determined under the fair value method for all awards | (604,259) | (507,347) | (2,304,112) | (1,400,648) |
| | (6,963,399) | (5,322,579) | (20,557,320) | (15,882,839) |
| Basic and diluted loss per share: | | | | |
| As reported | (0.24) | (0.21) | (0.69) | (0.67) |
| Pro forma | (0.26) | (0.23) | (0.77) | (0.73) |

The weighted-average fair value of options granted during the periods ended February 28, 2006 and 2005 were $8.95 and $13.43 respectively.

For purposes of calculating the compensation cost consistent with SFAS 123, the fair value of each option grant is estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in the periods ended February 28, 2006 and 2005:

| | FEBRUARY 28, 2006 | FEBRUARY 28, 2005 |
|---|---|---|
| Expected volatility ...... | 71.5% | 72.3% |
| Risk-free interest rate .. | 4.4% | 3.9% |
| Dividend yield .......... | -- | -- |
| Expected lives .......... | 7.0 years | 7.6 years |

========= =========

(5) RECENTLY ISSUED ACCOUNTING STANDARD

In December 2004, Statement of Financial Accounting Standards (SFAS) No. 123 (Revised 2004), "Share-Based Payment: an amendment of FASB Statements No. 123 and 95", was issued. This Statement amends SFAS No. 123, "Accounting for Stock-Based Compensation", and requires companies to recognize in the income statement the grant-date fair value of stock options and other equity-based compensation issued to employees. The Statement is effective for public companies with annual periods beginning after June 15, 2005. The Company will adopt SFAS

123(R) for the three-month period ending August 31, 2006. The Company will assess the impact of the transition to this new accounting standard during the upcoming months.

(6) MARKETABLE SECURITIES

The Company, at February 28, 2006, is invested in high grade commercial paper. The Company has the intent and ability to hold these securities until maturity and all securities have a maturity of less than one year.

The fair market value of the Company's marketable securities was $30,809,703 at February 28, 2006, which included gross unrealized holding losses of $378. The fair market value of the Company's marketable securities was $91,209,903 at May 31, 2005, which included gross unrealized holding losses of $120,386. All of these marketable securities are scheduled to mature in less than one year.

(7) LEGAL PROCEEDINGS

Subsequent to the end of the Company's fiscal third quarter, the Company and its chief executive officer were named as defendants in purported class action lawsuits pending before the federal District Court for the Northern District of Illinois alleging various violations of the federal securities laws. These lawsuits allege, among other matters, that the Company failed to adequately disclose information regarding the results from a clinical trial of its PolyHeme product in elective surgery that was conducted from 1998 to 2001. Although the Company believes these lawsuits lack merit, the lawsuits are at an early stage and it is not possible at this time to predict the outcome of any of the matters or their potential effect, if any, on the Company or the clinical development or future commercialization of its PolyHeme product.

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

RECENT DEVELOPMENTS

We are currently enrolling patients in a pivotal Phase III trial in which our PolyHeme(R) hemoglobin-based oxygen-carrying resuscitative fluid is being used for the first time in the U.S. to treat severely injured patients in hemorrhagic shock before they reach the hospital. Under this protocol, treatment with PolyHeme begins at the scene of the injury or in the ambulance and continues during transport and the initial 12-hour post-injury period in the hospital. Since blood is not presently carried in ambulances, the use of PolyHeme in this setting has the potential to improve survival and address a critical, unmet medical need.

Twenty-seven of the 32 clinical sites that have received Institutional Review Board, or IRB, approval to participate in our pivotal Phase III trial are enrolling patients in the trial. Thirty-one of these sites have initiated enrollment and the last is scheduled to open in April 2006. Three sites have suspended enrollment of patients in order to review their participation in the trial, and one site has suspended enrollment pending additional retraining. This review follows recent media reports that have challenged certain aspects of the design of our trial and the adequacy of the community consultation process conducted by clinical sites in connection with the trial. A number of other trial sites have conducted similar reviews and have already resumed their enrollment of patients in our trial.

Each of the sites participating in the trial is designated as a Level I trauma center, indicating its capacity to treat the most severely injured trauma patients. The trial has an expected enrollment of 720 patients.

As part of our trial protocol, an Independent Data Monitoring Committee, or IDMC, is responsible for periodically evaluating the safety data from the trial and making recommendations relating to the continuation or modification of the trial protocol to minimize any identified risks to patients. The IDMC has completed four separate evaluations after 60, 120, 250 and 500 patients were enrolled in our trial and monitored for a 30-day follow up period. The IDMC has stated that it observed no statistically significant trends or safety issues that would warrant modification or other changes in our current trial protocol or patient recruitment. Based on these observations, the IDMC has recommended that our trial continue to completion without modification. We will not have access to the trial data reviewed by the IDMC until the trial is completed and the database has been cleaned and locked by our contract research organization.

As of March 31, 2006, approximately 655 patients had been enrolled in our pivotal Phase III trial. Our current goal is to complete the patient enrollment phase in the second quarter of calendar year 2006. Our ability to achieve this goal will depend, in part, on the number of clinical sites continuing to participate in our trial and the ability of these sites to enroll patients at the projected rates.

The progress of our pivotal Phase III trial and the timing and outcome of the Food and Drug Administration, or FDA, review process are subject to significant risks and uncertainties, many of which are outside of our control. We urge you to review the "Risk Factors" section in our most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission for a discussion of certain of these risks and uncertainties.

Since Northfield's incorporation in 1985, we have devoted substantially all of our efforts and resources to the research, development and clinical testing of our potential product, PolyHeme. We have incurred operating losses during each year of our operations since inception and expect to incur substantial additional operating losses for the next several years. From Northfield's inception through February 28, 2006, we have incurred operating losses totaling $163,806,000.

We will be required to complete our pivotal Phase III trial and obtain FDA regulatory approval before PolyHeme can be sold commercially. The FDA regulatory process is subject to significant risks and uncertainties, and we therefore cannot at this time reasonably estimate the timing of any future revenues from

the commercial sale of PolyHeme. The costs incurred by Northfield to date and during each period presented below in connection with our development of

PolyHeme are described in the Statements of Operations in our financial statements.

Our success will depend on several factors, including our ability to obtain FDA regulatory approval of PolyHeme and our manufacturing facilities, obtain sufficient quantities of human red blood cells to manufacture PolyHeme in commercial quantities, manufacture and distribute PolyHeme in a cost-effective manner, enforce our patent positions and raise sufficient capital to fund these activities. We have experienced significant delays in the development and clinical testing of PolyHeme. We cannot ensure that we will be able to achieve these goals or that we will be able to realize product revenues or profitability on a sustained basis or at all.

## RESULTS OF OPERATIONS

We reported no revenues for either of the three and nine-month periods ended February 28, 2006 or 2005. From Northfield's inception through February 28, 2006, we have reported total revenues of $3,000,000, all of which were derived from licensing fees.

## OPERATING EXPENSES

Operating expenses for our third fiscal quarter ended February 28, 2006 totaled $7,240,000, an increase of $2,111,000 from the $5,129,000 reported in the third quarter of fiscal 2005. Measured on a percentage basis, third quarter fiscal 2006 operating expenses exceeded third quarter fiscal 2005 expenses by 41.2%. As expected, significant increases in operating expenses were incurred to conduct, expand, report and support our pivotal Phase III trial.

Research and development expenses during the third quarter of fiscal 2006 totaled $5,786,000, an increase of $1,968,000, or 51.5%, from the $3,818,000 reported in the third quarter of fiscal 2005. Our pivotal Phase III trial is enrolling patients at 10 additional clinical sites compared to a year ago. Also included in the current quarter research and development expenses was an increased use of scientific and regulatory consultants to prepare for the reporting of data from our trial to FDA.

General and administrative expenses in the third quarter of fiscal 2006 totaled $1,454,000, which is an increase of $143,000, or 10.9%, from the $1,311,000 of general and administrative expenses reported in the third quarter of fiscal 2005. The increased expenses in the third quarter of fiscal 2006 compared to the third quarter of fiscal year 2005 were due to increased professional service fees, compensation accruals, insurance costs, and state taxes determined by our capital structure. We anticipate potentially significant general and administrative expense increases for the remainder of the fiscal year. No new general and administrative programs are currently planned, as successfully completing our pivotal Phase III trial remains our primary focus. However, we anticipate potentially significant general and administrative expense increases for the remainder of the fiscal year due primarily to the proceedings discussed below.

Subsequent to the end of our fiscal third quarter, we received an informal request from the staff of the Securities and Exchange Commission, or SEC, to voluntarily provide certain information relating to the clinical development of PolyHeme in elective surgery. We intend to cooperate with the SEC staff in connection with its review of this information. We have also agreed to voluntarily provide similar information to the staff of the Finance Committee of the United States Senate. In addition, Northfield and our chief executive officer were named as defendants in purported class action lawsuits alleging violations of the federal securities laws relating to the disclosure of results from a clinical trial of our PolyHeme product in elective surgery that was conducted from 1998 to 2001. While we believe these lawsuits lack merit, each of these matters is at an early stage and it is not possible at this time to predict the outcome of any of the matters or their potential effect, if any, on Northfield or the clinical development or future commercialization of our PolyHeme product. See "Legal Proceedings." We anticipate significant future increases in our general and administrative expenses resulting from professional fees and expenses incurred in connection with these matters.

For the nine-month period ended February 28, 2006, operating expenses of $20,756,000 exceeded the operating expenses of $15,203,000 incurred in the nine-month period ended February 28, 2005. The dollar increase was $5,553,000 and the percentage increase equaled 36.5%. The increases are primarily attributed to the planning, preparation, execution, analysis and reporting of our pivotal Phase III trial.

Research and development expenses for the nine-month period ended February 28, 2006 totaled $16,454,000, which represents a $4,420,000, or 36.7%, increase from the comparable expenses incurred in the nine-month period ended February 28, 2005. During the current fiscal year, increased expense totaling $2,676,000 was reported for clinical site activities and the direct costs of trial monitoring, analysis and reporting. During the current fiscal year, the organization has expanded by 10 net hires contributing to increased compensation and recruiting costs. Also this fiscal year we are conducting additional work in multiple areas to refresh and update our database in preparation for filing a license application with FDA.

General and administrative expenses for the nine-month period ended February 28, 2006 totaled $4,303,000, which is an increase of $1,133,000, or 35.7%, from the $3,170,000 of general and administrative expenses reported for the nine-month period ended February 28, 2005. The increased expenses this fiscal year are due to higher employment levels, increased compensation accruals, higher professional services fees, primarily for legal and investor relations, increased insurance costs and additional taxes payable based on our increased market capitalization.

## INTEREST INCOME

Interest income for the three-month period ended February 28, 2006 totaled $845,000, an increase of $564,000 from the $281,000 in interest income reported in the three-month period ended February 28, 2005. The increase in our interest income is due to our improved cash position resulting from our successful equity financing during February 2005 and higher short-term interest rates.

Interest income for the nine-month period ended February 28, 2006 totaled $2,312,000, an increase of $1,755,000 from the $557,000 in interest income reported in the nine-month period ended February 28, 2005. The increase in cash balances and increases in available short-term interest rates caused interest income to increase. We continue to invest our funds only in high grade, short-term instruments.

## NET LOSS

Our net loss for the three-month period ended February 28, 2006 totaled $6,395,000, or $0.24 per share, compared to a net loss of $4,848,000, or $0.21 per share, for the three-month period ended February 28, 2005. In dollar terms, the loss increased by $1,547,000 or 31.9%, primarily as a result of the increased expenses relating to our pivotal Phase III trial.

On a fiscal year to date basis, we reported a loss of $18,445,000, or $0.69 per share, compared to a prior year nine-month loss of $14,646,000, or $0.67 per share. The increased net loss of $3,799,000, or 25.9%, was primarily the result of increased expenses relating to our pivotal Phase III trial during the first nine-months of the current fiscal year.

LIQUIDITY AND CAPITAL RESOURCES

From Northfield's inception through February 28, 2006, we have used cash in operating activities and for the purchase of property, plant, equipment and engineering services in the amount of $160,874,000. For the nine-months ended February 28, 2006 and February 28, 2005, these cash expenditures totaled $19,240,000 and $14,540,000, respectively. The current fiscal year nine-month increase in cash utilization is due primarily to increased expenses related to our pivotal Phase III trial and professional service costs.

We have financed our research and development and other activities to date through the public and private sale of equity securities and, to a more limited extent, through the license of product rights. As of February 28, 2006, we had cash and marketable securities totaling $80,313,000. As previously reported, we have been successful in securing a $1.4 million federal appropriation as part of the Defense Appropriation Bill in 2005 and a $3.5 million federal appropriation as part of the Fiscal 2006 Defense Appropriation Bill. As of February 28, 2006, we have not yet received these funds.

We are currently utilizing our cash resources at a rate of approximately $28 million per year. We expect, however, that the rate at which we utilize of our cash resources will significantly increase over the next two years as we launch our planned commercial plant expansion and further expand our business organization for product launch.

We anticipate that our expenditures for site monitoring and patient enrollment in connection with our current Phase III clinical trial will be completed in calendar 2006, while substantial additional costs will be incurred during calendar 2006 to complete and submit a Biologics License Application for PolyHeme with FDA. We also expect to incur additional expenses as we build manufacturing, sales, marketing and distribution capabilities in support of the commercialization of PolyHeme.

Based on our current estimates, we believe our existing capital resources will be sufficient to permit us to conduct our operations, including the planned expansion of our manufacturing, sales, marketing and distribution capabilities, for approximately 15 to 18 months. Excluding the projected costs relating to our planned expansion activities, we believe our existing capital resources would be sufficient to permit us to conduct our operations, including completion of our current Phase III clinical trial and the preparation and submission of a BLA to FDA, for approximately 30 to 36 months.

We may in the future issue additional equity or debt securities or enter into collaborative arrangements with strategic partners, which could provide us with additional funding or absorb expenses we would otherwise be required to pay. We are also pursuing potential sources of additional government funding. Any one or a combination of these sources may be utilized to raise additional capital. We believe our ability to raise additional capital or enter into a collaborative arrangement with a strategic partner will depend primarily on the results of our clinical trial, as well as general conditions in the business and financial markets.

Our capital requirements may vary materially from those now anticipated because of the timing and results of our clinical testing of PolyHeme, the establishment of relationships with strategic partners, changes in the scale, timing or cost of our planned commercial manufacturing facility, competitive and technological advances, the FDA regulatory process, changes in our marketing and distribution strategy and other factors.

## CRITICAL ACCOUNTING POLICIES

The preparation of financial statements requires management to make estimates and assumptions that affect amounts reported therein. We believe the following critical accounting policy reflects our more significant judgments and estimates used in the preparation of our financial statements.

### NET DEFERRED TAX ASSETS VALUATION

We record our net deferred tax assets in the amount that we expect to realize based on projected future taxable income. In assessing the appropriateness of our valuation, assumptions and estimates are required, such as our ability to generate future taxable income. In the event we were to determine that it was more likely than not we would be able to realize our deferred tax assets in the future in excess of their carrying value, an adjustment to recognize the deferred tax assets would increase income in the period such determination was made. As of February 28, 2006, we have recorded a 100% percent valuation allowance against our net deferred tax assets.

## CONTRACTUAL OBLIGATIONS

The following table reflects a summary of our contractual cash obligations as of February 28, 2006:

| Contractual Obligations | TOTAL | LESS THAN ONE YEAR | 1-3 YEARS | 4-5 YEARS |
|---|---|---|---|---|
| Lease Obligations (1) .......... | $2,866,402 | $ 834,799 | $1,788,683 | $242,920 |
| Other Obligations (2) .......... | 1,300,000 | 1,300,000 | -- | -- |
| Total Contractual Cash Oblig ... | $4,166,402 | $2,134,799 | $1,788,683 | $242,920 |

----------

(1) The lease for our Evanston headquarters is cancelable with six months notice combined with a termination payment equal to three months base rent at any time after February 14, 2009. If the lease is cancelled as of February 15, 2009 unamortized broker commissions of $17,470 would also be due.

(2) Represents payments required to be made upon termination of employment agreements with two of our executive officers. The employment contracts renew automatically unless terminated. Figures shown represent compensation payable upon the termination of the employment agreements for reasons other than death, disability, cause or voluntary termination of employment by the executive officer other than for good reason. Additional payments may be required under the employment agreements in connection with a termination of employment of the executive officers following a change in control of Northfield.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

We currently do not have any foreign currency exchange risk. We invest our cash and cash equivalents in government securities, certificates of deposit and money market funds. These investments are subject to interest rate risk. However, due to the nature of our short-term investments, we believe that the financial market risk exposure is not material. A one percentage point decrease in the interest rate received on our cash and marketable securities of $80.3 million at February 28, 2006 would decrease interest income by $803,000 on an annual basis.

ITEM 4. CONTROLS AND PROCEDURES.

Based on their evaluation as of the end of the period covered by this report, our Chief Executive Officer and Senior Vice President and Chief Financial Officer have concluded that Northfield's disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. There were no changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

On March 13, 2006, Northfield received an informal request from the staff of the SEC to voluntarily provide certain information relating to the clinical development of PolyHeme in elective surgery. We intend to cooperate with the SEC staff in connection with its review of this information. We have also agreed to voluntarily provide similar information to the staff of the Finance Committee of the United States Senate.

In addition, Northfield and our chief executive officer have been named as defendants in purported class action lawsuits pending before the federal District Court for the Northern District of Illinois alleging various violations of the federal securities laws. These lawsuits allege, among other matters, that Northfield failed to adequately disclose information regarding the results from a clinical trial of our PolyHeme product in elective surgery that was conducted from 1998 to 2001.

While we believe these lawsuits lack merit, each of these matters is at an early stage and it is not possible at this time to predict the outcome of any of the matters or their potential effect, if any, on Northfield or the clinical development or future commercialization of our PolyHeme product.

ITEM 6. EXHIBITS

a) Exhibit 15 - Letter RE: unaudited interim financial information

Exhibit 31.1 - Certification of Steven A. Gould, M.D., pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934

Exhibit 31.2 - Certification of Jack J. Kogut, pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934

Exhibit 32.1 - Certification of Steven A. Gould, M.D., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 32.2 - Certification of Jack J. Kogut, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

b) None

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company in the capacities indicated on April 10, 2006.

| SIGNATURE | TITLE |
| --- | --- |
| /s/ Steven A. Gould, M.D.<br>Steven A. Gould, M.D. | Chairman of the Board and Chief Executive Officer |
| /s/ Jack J. Kogut<br>Jack J. Kogut | Sr. Vice President and Chief Financial Officer |