

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

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended June 30, 2012

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: 000-53071

**TARGETED MEDICAL PHARMA, INC.**

(Exact name of registrant as specified in its charter)

Delaware

\_\_\_\_\_  
(State or other jurisdiction of Incorporation or organization)

20-5863618

\_\_\_\_\_  
(I.R.S. Employer Identification No.)

2980 Beverly Glen Circle  
Los Angeles, California

\_\_\_\_\_  
(Address of principal executive offices)

90077

\_\_\_\_\_  
(Zip Code)

(310) 474-9809

\_\_\_\_\_  
(Registrant's telephone number, including area code)

\_\_\_\_\_  
(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: As of August 14, 2012, there were 22,049,976 shares of common stock, par value \$0.001 per share, of the Registrant outstanding.

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PART I. FINANCIAL INFORMATION

TARGETED MEDICAL PHARMA, INC.  
CONSOLIDATED BALANCE SHEETS  
June 30, 2012 and December 31, 2011

	June 30, 2012 (Unaudited)	December 31, 2011
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and Cash Equivalents	\$ 44,603	\$ 147,364
Inventory	1,140,635	495,821
Accounts Receivable	568,302	899,493
Loans Receivable – Employees	92,688	23,360
Prepaid Expenses - Short Term	676,587	241,208
Prepaid Taxes	894,301	792,301
Deferred Tax Asset - Short Term	301,626	300,170
Total Current Assets	<u>3,718,742</u>	<u>2,899,717</u>
Property and Equipment - Net of Accumulated Depreciation	422,274	411,823
Intangible Assets - Net of Accumulated Amortization	2,365,237	2,387,801
Prepaid Expenses - Long Term	81,245	111,259
Deferred Tax Asset - Long Term	4,606,052	3,141,176
Other Assets	26,000	26,000
Total Assets	<u>\$ 11,219,550</u>	<u>\$ 8,977,776</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)</b>		
<b>Liabilities:</b>		
Accounts Payable and Accrued Expenses	\$ 5,897,038	\$ 5,035,136
Notes Payable-Related Parties net of \$0 and \$591,702 discount on warrants issued as of June 30, 2012 and December 31, 2011	5,227,000	1,775,561
Other Amounts due to Related Parties	585,448	602,948
Deferred Tax Liability - Current	69,648	69,648
Total Current Liabilities	<u>11,779,134</u>	<u>7,483,293</u>
Deferred Income Taxes	943,234	887,050
Total Liabilities	<u>12,722,368</u>	<u>8,370,343</u>
<b>Shareholders' Equity:</b>		
Preferred stock, \$0.001 par value; 20,000,000 shares authorized, no shares issued and outstanding	-	-
Common stock, \$0.001 par value; 100,000,000 shares authorized, 21,949,576 and 21,949,576 shares issued and outstanding at June 30, 2012 and December 31, 2011, respectively	21,950	21,950
Additional Paid-In Capital	6,374,584	4,684,095
Accumulated Deficit	(7,899,352)	(4,098,612)
Total Shareholders' Equity	<u>(1,502,818)</u>	<u>607,433</u>
Total Liabilities and Shareholders' Equity (Deficit)	<u>\$ 11,219,550</u>	<u>\$ 8,977,776</u>

The accompanying notes are an integral part of these financial statements.

**TARGETED MEDICAL PHARMA, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
**Three Months and Six Months ended June 30, 2012 and 2011**  
**(Unaudited)**

	Three Months ended		Six Months ended	
	June 30, 2012	Restated June 30, 2011	June 30, 2012	Restated June 30, 2011
<b>Revenues:</b>				
Product Sales	\$ 1,331,005	\$ 2,149,948	\$ 2,603,815	\$ 4,031,325
Service Revenue	<u>117,221</u>	<u>224,984</u>	<u>219,596</u>	<u>378,932</u>
Total Revenue	1,448,226	2,374,932	2,823,411	4,410,257
<b>Cost of Sales:</b>				
Cost of Product Sold	179,678	258,273	\$ 369,671	541,933
Cost of Services Sold	<u>441,582</u>	<u>297,123</u>	<u>886,324</u>	<u>670,462</u>
Total Cost of Sales	621,260	555,396	1,255,995	1,212,395
Total Gross Profit	<u>826,966</u>	<u>1,819,536</u>	<u>1,567,416</u>	<u>3,197,862</u>
<b>Operating Expenses:</b>				
Research and Development	30,009	32,372	\$ 57,273	69,120
Selling, General and Administrative	<u>2,494,018</u>	<u>2,696,893</u>	<u>4,778,372</u>	<u>5,560,861</u>
Total Operating Expenses	<u>2,524,027</u>	<u>2,729,265</u>	<u>4,835,645</u>	<u>5,629,981</u>
Net Income (Loss) before Other Income and Expense	(1,697,061)	(909,729)	(3,268,229)	(2,432,119)
<b>Other Income and Expense:</b>				
Interest Income (Expense)	(1,866,818)	-	\$ (1,942,657)	-
Investment Income (Loss)	<u>-</u>	<u>13</u>	<u>-</u>	<u>7,638</u>
Total Other Income and (Expense)	(1,866,818)	13	(1,942,657)	7,638
Net Income (Loss) before Taxes	(3,563,879)	(909,716)	(5,210,886)	(2,424,481)
Deferred Income Tax Expense (Benefit)	<u>(739,056)</u>	<u>(338,185)</u>	<u>(1,410,146)</u>	<u>(924,160)</u>
Net Income (Loss) before Comprehensive Income	(2,824,823)	(571,531)	(3,800,740)	(1,500,321)
Reclassification for losses included in Net Income	<u>-</u>	<u>-</u>	<u>-</u>	<u>(3,209)</u>
Comprehensive Income (Loss)	<u>\$ (2,824,823)</u>	<u>\$ (571,531)</u>	<u>\$ (3,800,740)</u>	<u>\$ (1,503,530)</u>
Basic and Diluted Loss Per Share	\$ (0.13)	\$ (0.03)	\$ (0.17)	\$ (0.07)
<b>Basic and Diluted Weighted Average Number of Common Shares</b>				
Outstanding	21,949,576	21,949,576	21,949,576	21,328,175

The accompanying notes are an integral part of these financial statements.

**TARGETED MEDICAL PHARMA, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
**Year ended December 31, 2011 and Six Months ended June 30, 2012**  
**(Unaudited)**

	Number of Shares of Common Stock	Amount	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
Balance - January 1, 2011 (1)-Restated	18,308,576	18,309	3,191,314	78,438	3,209	3,291,270
Stock Issued for Services	16,000	16	40,784	-	-	40,800
Shares issued to existing shell shareholders in the reorganization	3,625,000	3,625	(503,625)	-	-	(500,000)
Reclassification of Gains to Net Income	-	-	-	-	(3,209)	(3,209)
Warrants Issued in connection with loans from related party	-	-	591,702	-	-	591,702
Stock Option Expense	-	-	1,363,920	-	-	1,363,920
Net Loss	-	-	-	(4,177,050)	-	(4,177,050)
Balance - December 31, 2011	21,949,576	\$ 21,950	\$ 4,684,095	\$ (4,098,612)	\$ -	\$ 607,433
Warrants Issued in connection with loans from related party	-	-	1,301,457	-	-	1,301,457
Stock Option Expense	-	-	389,032	-	-	389,032
Net Loss	-	-	-	(3,800,740)	-	(3,800,740)
Balance - June 30, 2012	21,949,576	\$ 21,950	\$ 6,374,584	\$ (7,899,352)	\$ -	\$ (1,502,818)

- (1) The stockholders' equity has been recapitalized to give effect to the shares exchanged by existing shareholders pursuant to the merger agreement dated January 31, 2011, more fully discussed in Note 6 to these financial statements.

The accompanying notes are an integral part of these financial statements.

**TARGETED MEDICAL PHARMA, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
Six Months ended June 30, 2012 and 2011  
(Unaudited)

	Six Months ended June 30,	
	2012	Restated 2011
<b>Cash Flows from Operating Activities:</b>		
Net Income	\$ (3,800,740)	(1,500,321)
<b>Adjustments:</b>		
Depreciation and Amortization	223,291	215,766
Stock Option Compensation	389,032	530,973
Stock Issued for Services	-	40,800
Deferred Income Taxes	(1,410,146)	(924,160)
Amortization of Note Discount	1,942,657	-
<b>Changes:</b>		
Inventory	(644,814)	3,861
Accounts Receivable	331,191	(248,229)
Loans Receivable - Employees	(69,328)	(153,442)
Prepaid Expenses	(405,365)	3,888
Prepaid Taxes	(102,000)	191,723
Deferred Tax Asset	(130,947)	-
Other Assets	-	-
Accounts Payable and Accrued Expenses	861,902	863,530
Taxes Payable	-	-
Deferred Tax Liability	56,184	56,603
Net Cash Flows from Operating Activities	<u>(2,759,083)</u>	<u>(919,008)</u>
<b>Cash Flows from Investing Activities:</b>		
Net Sales or (Purchases) of Investments	-	241,207
Acquisition of Intangible Assets	(102,255)	(369,172)
Purchases of Property and Equipment	(108,923)	(66,651)
Net Cash Flows from Investing Activities	<u>(211,178)</u>	<u>(194,616)</u>
<b>Cash Flows from Financing Activities:</b>		
Notes Payable-Related Parties	2,885,000	450,000
Due to Related Parties	(17,500)	-
Net Cash Flows from Financing Activities	<u>2,867,500</u>	<u>450,000</u>
Net Change in Cash and Cash Equivalents	(102,761)	(663,624)
Cash and Cash Equivalents - Beginning of Year	147,364	795,914
Cash and Cash Equivalents - End of Period	<u>\$ 44,603</u>	<u>\$ 132,290</u>

**Supplemental Disclosure of Cash Flow Information**

Interest Paid	-	-
Interest Expense	-	10,400
Income Taxes Paid	102,000	152,675

**Supplemental Disclosure of Non-Cash Investing and Financing Activities**

On January 31, 2011 the Company issued a note payable to the Company's Founders in the amount of \$440,000 in partial payment of the \$500,000 stock purchase of the shell company.

The remaining \$60,000 is included in Accrued Expenses.

The accompanying notes are an integral part of these financial statements.

## Notes to Condensed Consolidated Financial Statements

### Note 1: Business Activity

TARGETED MEDICAL PHARMA, INC. (“Company”), also doing business as Physician Therapeutics (“PTL”), is a specialty pharmaceutical company that develops and commercializes nutrient- and pharmaceutical-based therapeutic systems. The Company also does business as Laboratory Industry Services (“LIS”), which is a facility for the performance of diagnostic testing. On July 30, 2007, the Company formed the wholly-owned subsidiary, Complete Claims Processing, Inc. (“CCPI”), which provides billing and collection services on behalf of physicians for claims to insurance companies, governmental agencies and other medical payers.

#### Segment Information:

The Company had revenue outside of the United States of \$0 and \$93,684 for the six months ended June 30, 2012 and 2011, respectively. The Company’s operations are organized into two reportable segments: Targeted Medical Pharma (“TMP”) and CCPI.

- TMP: This segment includes PTL and LIS as described above. This segment develops and distributes nutrient based therapeutic products and distributes pharmaceutical products from other manufacturers through employed sales representatives and distributors. TMP also performs the administrative, regulatory compliance, sales and marketing functions of the corporation, owns the corporation’s intellectual property and is responsible for research and development relating to medical food products and the development of software used for the dispensation and billing of medical foods, generic and branded products. The TMP segment also manages contracts and chargebacks.
- CCPI: This segment provides point-of-care dispensing solutions and billing and collections services. It is responsible for the research and development of billing software and methodologies and the customization of hardware that supports dispensing, billing and collection operations.

**Segment Information for the three months ended June 30,**

2012 (unaudited)	Total	TMP	CCPI
Gross Sales	\$ 1,448,226	\$ 1,331,005	\$ 117,221
Gross Profit (Loss)	\$ 826,966	\$ 1,151,327	\$ (324,361)
Comprehensive Income (Loss)	\$ (2,824,823)	\$ (2,500,462)	\$ (324,361)
Total Assets	\$ 11,219,550	\$ 11,459,574	\$ (240,024)
less Eliminations	\$ -	\$ (210,231)	\$ 210,231
Net Total Assets	<u>\$ 11,219,550</u>	<u>\$ 11,249,343</u>	<u>\$ (29,793)</u>

2011 (Unaudited and restated)	Total	TMP	CCPI
Gross Sales	\$ 2,374,932	\$ 2,149,948	\$ 224,984
Gross Profit	\$ 1,819,536	\$ 1,891,675	\$ (72,139)
Comprehensive Income	\$ (571,531)	\$ (172,548)	\$ (398,983)
Total Assets	\$ 6,367,070	\$ 9,040,723	\$ (2,673,653)
less Eliminations	\$ -	\$ (2,734,661)	\$ 2,734,661
Net Total Assets	<u>\$ 6,367,070</u>	<u>\$ 6,306,062</u>	<u>\$ 61,008</u>

**Segment Information for the six months ended June 30,**

2012 (unaudited)	Total	TMP	CCPI
Gross Sales	\$ 2,823,411	\$ 2,603,815	\$ 219,596
Gross Profit (Loss)	\$ 1,567,416	\$ 2,234,144	\$ (666,728)
Comprehensive Income (Loss)	\$ (3,800,740)	\$ (3,134,012)	\$ (666,728)
Total Assets	\$ 11,219,550	\$ 11,459,574	\$ (240,024)
less Eliminations	\$ -	\$ (210,231)	\$ 210,231
Net Total Assets	<u>\$ 11,219,550</u>	<u>\$ 11,249,343</u>	<u>\$ (29,793)</u>

2011 (Unaudited and restated)	Total	TMP	CCPI
Gross Sales	\$ 4,410,257	\$ 4,031,325	\$ 378,932
Gross Profit	\$ 3,197,862	\$ 3,489,392	\$ (291,530)
Comprehensive Income	\$ (1,503,530)	\$ (1,620,516)	\$ 116,986
Total Assets	\$ 6,367,070	\$ 9,040,723	\$ (2,673,653)
less Eliminations	\$ -	\$ (2,734,661)	\$ 2,734,661
Net Total Assets	<u>\$ 6,367,070</u>	<u>\$ 6,306,062</u>	<u>\$ 61,008</u>

**Note 2: Summary of Significant Accounting Policies**

Going concern: – The 2011 audited consolidated financial statements were prepared on the basis that the Company would continue as a going concern. The Company has losses for the year ended December 31, 2011 totaling \$4,177,050 as well as accumulated deficit amounting to \$4,491,740. Further the Company appeared to have inadequate cash and cash equivalents of \$147,364 as of December 31, 2011 to cover projected operating costs for the next 12 months. The loss for the six months ended June 30, 2012 was \$3,800,740, which increased the accumulated deficit to \$(7,899,352). As a result, the Company is dependent upon further financing, development of revenue streams with shorter collection times and accelerating collections on our physician managed and hybrid revenue business models.

These factors raise substantial doubt about the ability of the Company to continue as a going concern. The consolidated financial statements do not include any adjustments that might result from the outcome of these uncertainties. In this regard, management is planning to raise any necessary additional funds through loans and/or additional sales of its common stock development of revenue streams with shorter collection times and accelerating collections on our physician managed and hybrid revenue streams. There is no assurance that the Company will be successful in raising additional capital.

Principles of consolidation: The consolidated financial statements include accounts of TMP and its wholly owned subsidiary, CCPI, collectively referred to as “the Company”. All significant intercompany accounts and transactions have been eliminated in consolidation. In addition, TMP and CCPI share the common operating facility, certain employees and various costs. Such expenses are principally paid by TMP. Due to the nature of the parent and subsidiary relationship, the individual financial position and operating results of TMP and CCPI may be different from those that would have been obtained if they were autonomous.

Accounting estimates: The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.



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Cash Equivalents: The Company considers all highly liquid investments purchased with an original or remaining maturity of three months or less when purchased to be cash equivalents. The recorded carrying amounts of the Company's cash and cash equivalents approximate their fair market value.

Considerations of credit risk: Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade accounts receivable.

TMP markets medical foods and generic and branded pharmaceuticals through employed sales representatives, independent distributors and pharmacies. Product sales are invoiced upon shipment at Average Wholesale Price ("AWP"), which is a commonly used term in the industry, with varying rapid pay discounts, under four models: Physician Direct Sales, Distributor Direct Sales, Physician Managed and Hybrid.

Revenue Recognition:

Under the following revenue models product sales are invoiced upon shipment:

- *Physician Direct Sales Model* (1% of revenue for the six months ended June 30, 2012): Under this model, a physician purchases products from TMP but does not retain CCPI's services. TMP invoices the physician upon shipment under terms which allow a significant rapid pay discount off AWP for payment within discount terms in accordance with the product purchase agreement. The physicians dispense the product and perform their own claims processing and collections. TMP recognizes revenue under this model on the date of shipment at the gross invoice amount less the anticipated rapid pay discount offered in the product purchase agreement. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% may be applied to the outstanding balance. The physician is responsible for payment directly to TMP.
- *Distributor Direct Sales Model* (36% of revenue for the six months ended June 30, 2012): Under this model, a distributor purchases products from TMP and sells those products to a physician and the physician does not retain CCPI's services. TMP invoices distributors upon shipment under terms which include a significant discount off AWP. TMP recognizes revenue under this model on the date of shipment at the net invoice amount. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% may be applied to the outstanding balance.

Due to substantial uncertainties as to the timing and collectability of revenues derived from our Physician Managed and Hybrid models described below, which can take in excess of four years to collect, we have determined that these revenues did not meet the criteria for recognition in accordance with ASC 605, *Revenue Recognition*. These revenues are therefore required to be recorded when collectability is reasonably assured, which the Company has determined is when the payment is received.

- *Physician Managed Model* (45% of revenue for the six months ended June 30, 2012): Under this model, a physician purchases products from TMP and retains CCPI's services. TMP invoices physician upon shipment to physician under terms which allow a significant rapid pay discount for payment received within terms in accordance with the product purchase agreement which includes a security interest for TMP in the products and receivables generated by the dispensing of the products. The physician also executes a billing and claims processing services agreement with CCPI for billing and collection services relating to our products (discussed below). CCPI submits a claim for reimbursement on behalf of the physician client. The CCPI fee and product invoice amount are deducted from the reimbursement received by CCPI on behalf of the physician client before the reimbursement is forwarded to the physician client. In the event the physician fails to pay the product invoice within the agreed term, we can deduct the payment due from any of the reimbursements received by us on behalf of the physician client as a result of the security interest we obtained in the products we sold to the physician client and the receivables generated by selling the products in accordance with our agreement. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% is applied to the outstanding balance. However, since we are in the early stage of our business, as a courtesy to our physician clients, our general practice has been to extend the rapid pay discount beyond the initial term of the invoice until the invoice is paid and not to apply a late payment fee to the outstanding balance. TMP recognizes revenue under this model on the date payment is received at the gross invoice amount less the applicable rapid pay discount offered in the product purchase agreement

- *Hybrid Model* (11% of revenue for the six months ended June 30, 2012): Under this model, a distributor purchase products from TMP and sell those products to a physician and the physician retains CCPI's services. TMP invoices distributors upon shipment under terms which allow a significant rapid pay discount for payment received within terms in accordance with the product purchase agreements. The physician client of the distributor executes a billing and claims processing services agreement with CCPI for billing and collection services (discussed below). The distributor product invoice and the CCPI fee are deducted from the reimbursement received by CCPI on behalf of the physician client before the reimbursement is forwarded to the distributor for further delivery to their physician clients. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% is applied to the outstanding balance. However, since we are in the early stage of our business, as a courtesy to our physician clients, our general practice has been to extend the rapid pay discount beyond the initial term of the invoice until the invoice is paid and not to apply a late payment fee to the outstanding balance. TMP recognizes revenue under this model on the date payment is received at the net invoice amount.

In the six months ended June 30, 2012 and 2011 the Company issued invoices to Physician Managed and Hybrid model customers aggregating \$6,631,514 and \$8,430,195, respectively, which were not recognized as revenues or accounts receivable in the accompanying consolidated financial statements at the time of such billings. Direct costs associated with these revenues are expensed as incurred. Direct costs associated with these billings aggregating \$369,671 and \$541,933, respectively, were expensed in the accompanying consolidated financial statements at the time of such billings. However, in accordance with the revenue recognition policy described above, the Company recognized revenues from customers under these business models when cash was collected aggregating \$807,170 and \$1,234,060 in the six months ended June 30, 2012 and 2011, respectively. As of June 30, 2012, the Company had contractual receivables from its Physician Managed and Hybrid model customers totaling \$33,773,599 which are not reflected in the accompanying consolidated balance sheet as of such dates and will be recorded as revenue only when payment is received.

CCPI receives no revenue in the physician direct or distributor direct models because it does not provide collection and billing services to these customers. In the Physician Managed and Hybrid models, CCPI has a billing and claims processing service agreement with the physician. That agreement includes a service fee defined as a percentage of collections on all claims. Because fees are only earned by CCPI upon collection of the claim and the fee is not determinable until the amount of the collection of the claim is known, CCPI recognizes revenue at the time that collections are received.

No returns of products are allowed except products damaged in shipment, which has been insignificant.

The rapid pay discounts to the AWP offered to the physician or distributor, under the models described above, vary based upon the expected payment term from the physician or distributor. The discounts are derived from the Company's historical experience of the collection rates from internal sources and updated for facts and circumstances and known trends and conditions in the industry, as appropriate. As described in the models above, we recognize provisions for rapid pay discounts in the same period in which the related revenue is recorded. We believe that our current provisions appropriately reflect our exposure for rapid pay discounts. These rapid pay discounts, have typically ranged from 40% to 88% of Average Wholesale Price and we have monitored our experience ratio periodically over the prior twelve months and have made adjustments as appropriate.

Allowance for doubtful accounts: Under the direct sales to physician and direct sales to distributor models, product is sold under terms that allow substantial discounts (40-88%) for payment within terms. With such substantial discounts, it is rare that an invoice is not paid within terms. We have not experienced any write offs associated with these revenue models.

Under the Company's physician managed model and hybrid model, CCPI performs billing and collection services on behalf of the physician client and deducts the CCPI fee and product invoice amount from the reimbursement received by CCPI on behalf of the physician client before the reimbursement is forwarded to the physician client. Extended collection periods are typical in the workers compensation industry with payment terms extending from 45 days to in excess of four years. The physician remains personally liable for purchases of product from TMP and, during this long collection cycle, TMP retains a security interest in all products sold to the physician along with the claims receivable that result from sales of the products. CCPI maintains an accounting of all managed accounts receivable on behalf of the physician and regularly reports to the physician. As described above, due to uncertainties as to the timing and collectability of revenues derived from these models, revenue is recorded when payment is received therefore no allowance for doubtful accounts is necessary.

In addition to the bad debt recognition policy above, it is also TMP's policy to write down uncollectible loans and trade receivables when the payer is no longer in existence, is in bankruptcy or is otherwise insolvent. In such instances our policy is to reduce accounts receivable by the uncollectible amount and to proportionally reduce the allowance for doubtful accounts.

Inventory valuation: Inventory is valued at the lower of cost (first in, first out) or market and consists primarily of finished goods.

Property and equipment: Property and equipment are stated at cost. Depreciation is calculated using the straight line method over the estimated useful lives of the related assets. Computer equipment is amortized over three to five years. Furniture and fixtures are depreciated over five to seven years. Leasehold improvements are amortized over the shorter of fifteen years or term of the applicable property lease. Maintenance and repairs are expensed as incurred; major renewals and betterments that extend the useful lives of property and equipment are capitalized. When property and equipment is sold or retired, the related cost and accumulated depreciation are removed from the accounts and any gain or loss is recognized. Amenities are capitalized as leasehold improvements.

Impairment of long-lived assets: The long-lived assets held and used by the Company are reviewed for impairment no less frequently than annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In the event that facts and circumstances indicate that the cost of any long-lived assets may be impaired, an evaluation of recoverability is performed. No asset impairment was recorded for the six months ended June 30, 2012 or 2011.

Intangible assets: Intangible assets with finite lives, including patents and internally developed software (primarily the Company's *PDRx* Software), are stated at cost and are amortized over their useful lives. Patents are amortized on a straight line basis over their statutory lives, usually fifteen to twenty years. Internally developed software is amortized over three to five years. Intangible assets with indefinite lives are tested annually for impairment, during the fiscal fourth quarter and between annual periods, and more often when events indicate that an impairment may exist. If impairment indicators exist the intangible assets are written down to fair value as required. No asset impairment was recorded for the six months ended June 30, 2012 or 2011.

Fair value of financial instruments: The Company's financial instruments are accounts receivable, accounts payable and notes payable. The recorded values of accounts receivable, accounts payable, and notes payable approximate their values based on their short term nature.

Income taxes: The Company determines its income taxes under the asset and liability method. Under the asset and liability approach, deferred income tax assets and liabilities are calculated and recorded based upon the future tax consequences of temporary differences by applying enacted statutory tax rates applicable to future periods for differences between the financial statements carrying amounts and the tax basis of existing assets and liabilities. Generally, deferred income taxes are classified as current or non-current in accordance with the classification of the related asset or liability. Those not related to an asset or liability are classified as current or non-current depending on the periods in which the temporary differences are expected to reverse. Valuation allowances are provided for significant deferred income tax assets when it is more likely than not that some or all of the deferred tax assets will not be realized.

The Company recognizes tax liabilities by prescribing a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized, and also provides guidance on de-recognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The minimum threshold is defined as a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. To the extent that the final tax outcome of these matters is different than the amount recorded, such differences impact income tax expense in the period in which such determination is made. Interest and penalties, if any, related to accrued liabilities for potential tax assessments are included in income tax expense.

Stock-Based Compensation: The Company accounts for stock option awards in accordance with ASC 718. Under ASC 718, compensation expense related to stock-based payments is recorded over the requisite service period based on the grant date fair value of the awards. Compensation previously recorded for unvested stock options that are forfeited is reversed upon forfeiture. The Company uses the Black-Scholes option pricing model for determining the estimated fair value for stock-based awards. The Black-Scholes model requires the use of assumptions which determine the fair value of stock-based awards, including the option's expected term and the price volatility of the underlying stock.

The Company's accounting policy for equity instruments issued to consultants and vendors in exchange for goods and services follows the provisions of ASC 505-50. Accordingly, the measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant or vendor's performance is complete. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement.

Income Per Share: The Company utilizes ASC 260, "Earnings per Share". Basic income (loss) per share is computed by dividing income (loss) available to common shareholders by the weighted-average number of common shares outstanding. Diluted income (loss) per share is computed similar to basic income (loss) per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. Common equivalent shares are excluded from the computation if their effect is anti-dilutive.

The following potential common shares have been excluded from the computation of diluted net income (loss) per share for the periods presented where the effect would have been anti-dilutive:

	June 30, 2012	June 30, 2011
Options shares excluded	1,893,444	291,347

**Research and development:** Research and development costs are expensed as incurred. In instances where we enter into agreements with third parties for research and development activities we may prepay fees for services at the initiation of the contract. We record the prepayment as a prepaid asset and amortize the asset into research and development expense over the period of time the contracted research and development services are performed. Most contract research agreements include a ten year records retention and maintenance requirement. Typically, we expense 50% of the contract amount within the first two years of the contract and 50% over the remainder of the record retention requirements under the contract based on our experience on how long the clinical trial service is provided.

**Reclassification:**

Certain accounts in the prior-year consolidated financial statements have been reclassified for comparative purposes to conform to the presentation in the current-year financial statements.

**Note 3: Stock Based Compensation**

For the six months ended June 30, 2012 and 2011, the Company recorded compensation costs for options amounting to \$389,032 and \$530,973 respectively. A deduction is not allowed for income tax purposes until nonqualified options are exercised. The amount of this deduction will be the difference between the fair value of the Company's common stock and the exercise price at the date of exercise. Accordingly, there is a deferred tax asset recorded for the tax effect of the financial statement expense recorded. The tax effect of the income tax deduction in excess of the financial statement expense, if any, will be recorded as an increase to additional paid-in capital. No tax deduction is allowed for incentive stock options (ISO). Accordingly no deferred tax asset is recorded for GAAP expense related to these options.

Management has valued the options at their date of grant utilizing the Black Scholes option pricing model. As of the issuance of these consolidated financial statements, there was not a public market for the Company shares. Accordingly, the fair value of the underlying shares was determined based on the historical volatility data of similar companies, considering the industry, products and market capitalization of such other entities. The risk-free interest rate used in the calculations is based on the implied yield available on U.S. Treasury issues with an equivalent term approximating the expected life of the options depending on the date of the grant and expected life of the options. The expected life of the options used was based on the contractual life of the option granted. Stock-based compensation is a non-cash expense because we settle these obligations by issuing shares of our common stock from our authorized shares instead of settling such obligations with cash payments.

The fair value of options granted in the six months ended June 30, 2012 was determined using the following assumptions:

- Volatility factors of 83-84% were based on similar companies;
- Expected terms of 5.25-6 years based on one-half of the average of the vesting term and the ten year expiration of the option grant;
- A dividend rate of zero; and
- The risk free rate was the treasury rate with a maturity of the expected term (1.95% to 2.46%).

The following table summarizes the status of the Company's aggregate stock options granted:

	Number of Shares Remaining Options	Weighted Average Exercise Price
Outstanding at January 1, 2011	566,424	\$ 2.11
Options granted during 2011	1,382,538	\$ 2.96
Options exercised during 2011	0	
Options forfeited during 2011	365,871	\$ 2.62
Outstanding at December 31, 2011	1,583,091	\$ 2.73
Exercisable at December 31, 2011	1,147,909	\$ 2.49
Options granted during 2012	310,353	\$ 1.08
Options exercised during 2012	0	
Options forfeited during 2012	0	
Outstanding at June 30, 2012	1,893,444	\$ 2.46
Exercisable at June 30, 2012	1,538,052	\$ 2.48

The following table summarizes the status of the Company's aggregate non-vested shares:

	Number of Non-vested Shares	Weighted Average fair Value at Grant Date
Non-vested at December 31, 2010	206,310	\$ 1.07
Granted in 12 months ended December 31, 2011	1,382,538	\$ 2.10
Forfeited in 12 months ended December 31, 2011	365,871	\$ 1.76
Vested in 12 months ended December 31, 2011	941,599	\$ 1.61
Non-vested at December 31, 2011	435,182	\$ 1.66
Exercisable at December 31, 2011	1,147,909	\$ 1.30
Outstanding at December 31, 2011	1,583,091	\$ 1.40
Granted in six months ended June 30, 2012	310,353	\$ 0.44
Forfeited in six months ended June 30, 2012	-	\$ -
Vested in six months ended June 30, 2012	390,144	\$ 1.09
Non-vested at June 30, 2012	355,391	\$ 1.23
Exercisable at June 30, 2012	1,538,052	\$ 1.24
Outstanding at June 30, 2012	1,893,444	\$ 1.24

Per employment agreements with each of Dr. Shell and Mr. Giffoni (the "TMP Insiders"), each dated September 1, 2010 and amended on January 31, 2011, the TMP Insiders are entitled to 500,000 shares of common stock and annual base salary and benefits for the longer of the remaining term of the employment agreement or 30 months in the event the TMP Insider is terminated without cause by us or with cause by the TMP Insider. We would have "cause" to terminate the employment relationship upon (i) a TMP Insider's conviction of or a plea of nolo contendere for the commission of a felony or (ii) the TMP Insider's willful failure to substantially perform the TMP Insider's duties under the employment agreement. A TMP Insider will have "cause" to terminate the employment relationship with us in the event any of the following circumstances are not remedied within 30 days of our receipt of a notice of termination from the TMP Insider: (i) a material change in the TMP Insider's duties or a material limitation of the TMP Insider's powers; (ii) a failure to elect the TMP Insider to the management position specified in such TMP Insider's employment agreement or a reduction of the TMP Insider's annual base salary; (iii) our failure to continue in effect any benefit plan in effect upon the execution of the initial employment agreement, (iv) a material breach by us of the employment agreement and (v) a change in control (which is defined in the TMP Insiders' employment agreements). Amendment No. 1 to each of the TMP Insiders' employment agreements deleted the change in control provisions.

Pursuant to the employment agreements, the TMP Insiders are also entitled to receive incentive stock options ranging from 7,394 options to 110,917 options, each at an exercise price of \$3.49 per share (which numbers have been adjusted for the Reorganization), in the event we achieve certain EBITDA targets ranging from \$50,000,000 to \$250,000,000. The Company will grant additional incentive stock options upon achievement of each milestone set forth below. Milestone levels shall be based upon EBITDA reported in the financial statements during any calendar year. EBITDA is defined as earnings before taxes, interest, depreciation, and amortization.

<b>EBITDA</b>	<b>Options</b>
\$ 50,000,000	an option to purchase 5,000 shares Common Stock.
\$ 60,000,000	an option to purchase 7,500 shares Common Stock.
\$ 80,000,000	an option to purchase 7,500 shares Common Stock.
\$ 100,000,000	an option to purchase 10,000 shares Common Stock.
\$ 125,000,000	an option to purchase 10,000 shares Common Stock.
\$ 150,000,000	an option to purchase 10,000 shares Common Stock.
\$ 175,000,000	an option to purchase 15,000 shares Common Stock.
\$ 200,000,000	an option to purchase 50,000 shares Common Stock.
\$ 250,000,000	an option to purchase 75,000 shares Common Stock.

The fair value of warrants issued in connection with certain loans made by related parties during the three months ended June 30, 2012 was determined using the Black Scholes Option Pricing Model with the following assumptions:

- Stock price of \$0.612.55
- Exercise price of \$1.00
- Volatility factor of 96.66% based on similar companies;
- Expected term of 5 years based on the term of the warrant;
- A dividend rate of zero; and
- The risk free rate of 0.90%

The following table summarizes the status of the Company's outstanding warrants

Date	Note Amount	Interest Rate	Number of Warrants
08/19/11	\$ 150,000	3.95%	43,568
09/01/11	\$ 80,000	3.95%	23,237
09/23/11	\$ 52,000	3.95%	15,104
09/28/11	\$ 200,000	3.95%	58,091
10/17/2011	\$ 170,000	3.95%	50,296
10/20/2011	\$ 125,000	3.95%	36,982
11/8/2011	\$ 120,000	3.95%	35,503
11/22/2011	\$ 140,000	3.95%	41,420
12/7/2011	\$ 115,000	3.95%	34,024
1/4/2012	\$ 30,000	3.95%	8,876
1/18/2012	\$ 25,000	3.95%	7,396
1/19/2012	\$ 100,000	3.95%	29,586
1/31/2012	\$ 200,000	3.95%	59,172
2/1/2012	\$ 250,000	3.95%	73,964
2/15/2012	\$ 200,000	3.95%	59,172
2/29/2012	\$ 240,000	3.95%	71,006
3/15/2012	\$ 75,000	3.95%	22,189
3/28/2012	\$ 150,000	3.95%	44,379
4/11/2012	\$ 250,000	3.95%	250,000
4/19/2012	\$ 100,000	3.95%	100,000
4/26/2012	\$ 200,000	3.95%	200,000
5/2/2012	\$ 150,000	3.95%	150,000
5/10/2012	\$ 110,000	3.95%	110,000
5/24/2012	\$ 220,000	3.95%	220,000
5/25/2012	\$ 190,000	3.95%	190,000
6/13/2012	\$ 175,000	3.95%	175,000
6/27/2012	\$ 220,000	3.95%	220,000
	\$ 4,037,000		2,328,964

**Note 4: Notes Payable – Related Parties**

On December 12, 2010, the Company issued a promissory note to the Targeted Medical Pharma, Inc. Profit Sharing Plan (the "Plan") in the amount of \$300,000 (the "Plan Note"). The note bears interest at a rate of 8.0 percent per annum and was payable on June 12, 2011.

On January 31, 2011, the Company issued promissory notes to each of William Shell, our Chief Executive Officer, Chief Scientific Officer, interim Chief Financial Officer and a director, Elizabeth Charuvastra, our Chairman, Vice President of Regulatory Affairs and a director, and Kim Giffoni, our Executive Vice President of Foreign Sales and Investor Relations and a director, in an aggregate amount of \$440,000. The notes bear interest at a rate of 6% per annum and are payable on the earlier of December 1, 2012 or the consummation of the Company's initial public offering.

On May 4, 2011, the Company issued a promissory note to the Elizabeth Charuvastra and William Shell Family Trust dated July 27, 2006 and Amended September 29, 2006 (the "EC and WS Family Trust") in the amount of \$200,000. The note bears interest at a rate of 3.25% per annum and is payable May 14, 2016.

On May 4, 2011, the Company issued a promissory note to the Giffoni Family Trust Dated September 26, 2008 (the "Giffoni Family Trust") in the amount of \$100,000. The note bears interest at a rate of 3.25% per annum and is payable on demand.



On June 12, 2011, the Company, the Plan, William E. Shell, Elizabeth Charuvastra, Kim Giffoni, the EC and WS Family Trust and the Giffoni Family Trust entered into an agreement (the "Note Agreement") pursuant to which the Plan assigned the Plan Note to Dr. Shell, Ms. Charuvastra and Mr. Giffoni in an amount of \$100,000 each. Moreover, pursuant to the Note Agreement, each of Dr. Shell and Ms. Charuvastra assigned their respective interests in the Plan Note to the EC and WS Family Trust. In accordance with the Note Agreement, in connection with the assignments, the Plan Note was amended to extend the maturity date to December 15, 2015 and to reduce the interest rate from 8.0% per annum to 3.25% per annum. The Company issued new notes to each of the WC and WS Family Trust (in the amount of \$200,000) and to Mr. Giffoni (in the amount of \$100,000) to memorialize the amendments pursuant to the Note Agreement.

On June 18, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$150,000. The note bears interest at a rate of 3.25% per annum and is payable on demand.

August 19, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$150,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 43,568 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued November 7, 2011 and expires August 19, 2016.

On September 1, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$80,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 23,237 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued November 7, 2011 and expires September 1, 2016.

On September 23, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$52,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 15,104 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued November 7, 2011 and expires September 23, 2016.

On September 28, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$200,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 58,091 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued November 7, 2011 and expires September 28, 2016.

On October 17, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$170,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 50,296 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued October 17, 2011 and expires October 17, 2016.

On October 20, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$125,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 36,982 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued October 20, 2011 and expires October 20, 2016.

On November 8, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$120,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 35,503 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued November 8, 2011 and expires November 8, 2016.

On November 22, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$140,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 41,420 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued November 22, 2011 and expires November 22, 2016.

On December 7, 2011, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$115,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 34,024 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued December 7, 2011 and expires December 7, 2016.

On January 4, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$30,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 8,876 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share. This warrant was issued January 4, 2012 and expires January 4, 2017.

On January 18, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$25,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 7,396 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued January 18, 2012 and expires January 18, 2017.

On January 19, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$100,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 29,586 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued January 19, 2012 and expires January 19, 2017.

On January 31, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$200,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 59,172 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued January 31, 2012 and expires January 31, 2017.

On February 1, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$250,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 73,964 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued February 1, 2012 and expires February 1, 2017.

On February 15, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$200,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 59,172 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued February 15, 2012 and expires February 15, 2017.

On February 29, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$240,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 71,006 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued February 29, 2012 and expires March 1, 2017.

On March 15, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$75,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 22,189 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued March 15, 2012 and expires March 15, 2017.

On March 28, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$150,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 44,739 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$3.38 per share, This warrant was issued March 28, 2012 and expires March 28, 2017.

On April 11, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$250,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 250,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires April 11, 2017.

On April 19, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$100,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 100,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires April 19, 2017.

On April 26, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$200,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 200,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires April 26, 2017.

On May 2, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$150,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 150,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires May 2, 2017.

On May 10, 2012 the Company issued a promissory note to the EC and WS Family Trust in the amount of \$110,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 110,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires May 10, 2017.

On May 24, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$220,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 220,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires May 24, 2017.

On May 25, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$190,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 190,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires May 25, 2017.

On June 13, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$175,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 175,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 22, 2012 and expires June 13, 2017.

On June 22, 2012 the terms of all notes listed above to the EC and WS Family Trust were modified to make the principal payable on demand and accrued interest payable on a quarterly basis. The Company recorded any remaining note discount as of June 22, 2012.

On June 27, 2012, the Company issued a promissory note to the EC and WS Family Trust in the amount of \$220,000. The note bears interest at a rate of 3.95% per annum and is payable on demand. As an inducement to make this loan the EC and WS Family Trust was issued a warrant for 220,000 shares of Targeted Medical Pharma, Inc. common stock at an exercise price of \$1.00 per share, This warrant was issued June 27, 2012 and expires June 27, 2017.

As approved on July 27, 2012, warrants issued by the Company after June 30, 2012 will contain a provision such that if and whenever the Company shall either (i) reduce, or be deemed to have reduced, the exercise price or conversion price of any of its outstanding warrants to purchase shares of Common Stock of the Company, or any other security exercisable for, or convertible into, shares of Common Stock of the Company, to a price lower than the Exercise Price of the Warrant in effect immediately prior to the time of such reduction, or (ii) issues or sells, or is deemed to have issued or sold, any additional warrants to purchase shares of Common Stock of the Company, or any other security exercisable for, or convertible into, shares of Common Stock of the Company, with a price lower than the Exercise Price of the Warrant in effect immediately prior to the time of such issuance or sale, then, and in each such case, the then-existing Exercise Price of the Warrant shall be reduced to a price equal to the exercise price or conversion price of such amended or newly-issued or sold security.

#### **Note 5: Recently Issued Accounting Pronouncements**

**Presentation of Comprehensive Income:** In June 2011, the FASB issued ASU No. 2011-05, "Presentation of Comprehensive Income" (ASU 2011-05). The provisions of ASU 2011-05 amend FASB ASC Topic 220 "Comprehensive Income" to eliminate the current option to present the components of other comprehensive income in the statement of changes in equity, and require the presentation of net income and other comprehensive income (and their respective components) either in a single continuous statement or in two separate but consecutive statements. The amendments do not alter any current recognition or measurement requirements with respect to items of other comprehensive income. The provisions of ASU 2011-05 are effective for the Company's first reporting period beginning on January 1, 2012, with early adoption permitted. The adoption of ASU 2011-05 did not have a material impact on the Company's condensed consolidated financial statements.

**Fair Value Measurement and Disclosure:** In May 2011, the FASB issued ASC Update 2011-04, "Fair Value Measurement: (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs." ASC Update 2011-04 amends current U.S. GAAP to create more commonality with IFRS by changing some of the wording used to describe requirements for measuring fair value and for disclosing information about fair value measurements. This update is effective for the first interim or annual reporting period beginning after December 15, 2011. The Company began application of ASC 2011-04 on January 1, 2012, which is not expected to have any effect on results of operations, financial position, and cash flows.

## **Note 6: Reorganization**

Pursuant to an Agreement and Plan of Reorganization (the “Merger Agreement”), by and among AFH Acquisition III, Inc. (“AFH”), TMP Merger Sub, Inc. (“TMP Merger Sub”), AFH Merger Sub, Inc. (“AFH Merger Sub”), AFH Holding and Advisory, LLC (“AFH Advisory”), Targeted Medical Pharma, Inc. (“Old TMP”), William E. Shell, MD, Elizabeth Charuvastra and Kim Giffoni, on January 31, 2011, TMP Merger Sub merged (the “TMP Merger”) with and into Old TMP with Old TMP continuing as the surviving entity. Immediately after the TMP Merger, AFH merged (the “AFH Merger” and, together with the TMP Merger, the “Reorganization”) with and into AFH Merger Sub with AFH continuing as the surviving entity (the surviving entity of the AFH Merger, the “Subsidiary”). As a result of the Reorganization, the Subsidiary is the Company’s wholly-owned subsidiary.

Upon consummation of the TMP Merger, (i) each outstanding share of Old TMP common stock was exchanged for approximately 1.48 shares of AFH common stock and (ii) each outstanding TMP option, which was exercisable for one share of Old TMP common stock, was exchanged for an option exercisable for 1.48 shares of AFH common stock. Upon consummation of the AFH Merger, which occurred immediately upon consummation of the TMP Merger, each outstanding share of AFH common stock and each outstanding option to purchase AFH common stock were exchanged for one share of the Company’s common stock and one option to purchase one share of the Company’s common stock. As a result of the Reorganization, holders of Old TMP common stock and options received 18,308,576 of the Company’s shares of common stock and options to purchase 566,424 of the Company’s shares, or 83.89% of the Company’s issued and outstanding common stock on a fully diluted basis. Former shareholders of AFH Advisory received 3,625,000 of the Company’s shares of common stock.

The exchange of shares between TMP and AFH has been accounted for as a recapitalization of the companies. Pursuant to the accounting for a recapitalization, the historical carrying value of the assets and liabilities of TMP carried over to the surviving company. The reorganization was reflected in the statements as of the earliest period presented.

Pursuant to the Merger Agreement, the TMP Insiders agreed that up to 1,906,768 of the Company’s shares of common stock they hold in the aggregate would be subject to forfeiture and cancellation to the extent that the Company fails to achieve \$22,000,000 in Adjusted EBITDA (the “Make Good Target”) for the fiscal year ended December 31, 2011. For purposes of the Merger Agreement, “Adjusted EBITDA” means the Company’s consolidated net earnings before interest expense, income taxes, depreciation, amortization and non-recurring expenses (as defined below) for the applicable period and as calculated on a consistent basis. Net earnings excludes, among other things, expenses incurred in connection with the Company’s public offering of its common stock (including the preparation of the registration statement) and the preparation of the Current Report on Form 8-K related to the Reorganization.

On October 17, 2011, the Company, AFH Holding and Advisory, LLC, William E. Shell, MD, the Estate of Elizabeth Charuvastra and Kim Giffoni entered into Amendment No. 1 (the “Amendment”) to the Merger Agreement. Pursuant to the Amendment, the “Make Good Period” was changed from the fiscal year ended December 31, 2011 to the twelve months following the consummation of a financing resulting in gross proceeds of \$20 million to the Company.

On August 13, 2012, the Company, AFH Advisory, Dr. Shell, the Estate of Elizabeth Charuvastra (the “Estate”), our former Chairman and Vice President of Regulatory Affairs, and Mr. Giffoni (collectively Dr. Shell, the Estate and Mr. Giffoni, the “Insiders”) entered into Amendment No. 2 (“Amendment No. 2”) to the Agreement and Plan of Reorganization. Pursuant to Amendment No. 2, the make good provision, pursuant to which the Insiders had agreed to cancel up to 1,906,768 shares in the aggregate in the event stated EBITDA targeted were not achieved by the Company, has been deleted in its entirety.

Amounts due AFH resulting from this transaction totaling \$585,448 and \$602,948 as of June 30, 2012 and December 31, 2011 respectively are reflected as Other Amounts due to Related Parties.

## **Note 7: Subsequent Events**

Since June 30, 2012, the EC and WS Family Trust has made additional loans to the Company in the aggregate amount of \$290,000. In connection with such loans, the Company issued to the EC and WS Family Trust five year demand notes bearing interest at 3.95 percent per annum and five-year warrants to purchase 290,000 shares of the Company’s common stock at an exercise price of \$1.00 per share.

Effective July 20, 2012, the Company and AFH Holding and Advisory, LLC (“AFH Advisory”) entered into a letter agreement (the “Letter Agreement”) which was supplemented July 25, 2012 which details the parties agreement and supersedes all earlier agreements between the parties. The parties agreed as follows:

1. **Form 211.** “AFH Advisory” shall assist and advise the Company and its affiliates in facilitating the quotation of the Company’s shares of common stock on the OTC Bulletin Board by identifying and helping the Company to engage the necessary market maker to file a Form 211, or 15c2-11 Exemption Form as applicable, with the Financial Industry Regulatory Authority (“FINRA”).
2. **No Share Forfeiture and Continuing Registration Rights.** AFH Advisory has, and shall continue to have, normal and customary piggyback registration rights with respect to its shares of common stock, as further set forth in the Registration Rights Agreement, dated January 31, 2011. AFH Advisory and its affiliates will no longer be required to forfeit shares as a result of the failure to complete a financing.

3. **Reimbursement of Costs.** AFH Advisory is entitled to a reimbursement of \$585,448 of expenses incurred on behalf of the Company in connection with the Business Combination, and related matters (the “Expense Reimbursement Amount”). Concurrently with the execution of this New Agreement, the Company shall issue to AFH Advisory a Secured Convertible Promissory Note in the principal amount equal to the Expense Reimbursement Amount with interest payable quarterly in arrears at a rate of 8.5% per annum. A Security Agreement was also entered into with AFH effective July 20, 2012 assigning certain assets of the Company to AGH as collateral for the Promissory Note. The \$585,448 may be offset by \$250,000 or any remaining portion thereof relating to payments advanced to AFH Advisory by the Company in connection with a contemplated asset-based loan.
4. **Warrants.** In partial consideration for its services in connection with the Business Combination, upon the approval of the Company’s Board of Directors, the Company shall issue to AFH Advisory five-year warrants to purchase 1,063,981 shares of common stock of the Company (the “Warrant Stock”), at an exercise price of \$1.00 per share. If and whenever the Company shall either (i) reduce, or be deemed to have reduced, the exercise price or conversion price of any of its outstanding warrants to purchase shares of Common Stock of the Company, or any other security exercisable for, or convertible into, shares of Common Stock of the Company, to a price lower than the Exercise Price of the Warrant in effect immediately prior to the time of such reduction, or (ii) issues or sells, or is deemed to have issued or sold, any additional warrants to purchase shares of Common Stock of the Company, or any other security exercisable for, or convertible into, shares of Common Stock of the Company, with a price lower than the Exercise Price of the Warrant in effect immediately prior to the time of such issuance or sale, then, and in each such case, the then-existing Exercise Price of the Warrant shall be reduced to a price equal to the exercise price or conversion price of such amended or newly-issued or sold security.
5. **Board Oversight.** For a period of two (2) years following the date hereof, AFH Advisory shall have a right to disapprove two nominees for director chosen by the board of directors.
6. **Advisory Role.** For a period of two (2) years from the date of this letter agreement, AFH Advisory has the non-exclusive right to act as advisor to the Company on any proposed financings and/or mergers and acquisitions, to be separately engaged on a deal by deal basis at the Company’s discretion with respect to any specific transaction, the Company may choose not to retain AFH and Advisory as an advisor.

On August 13, 2012, the Company, AFH Advisory, Dr. Shell, the Estate and Mr. Giffoni entered into Amendment No. 2 to the Agreement and Plan of Reorganization. Pursuant to Amendment No. 2, the make good provision, pursuant to which the Insiders had agreed to cancel up to 1,906,768 shares in the aggregate in the event stated EBITDA targeted were not achieved by the Company, has been deleted in its entirety.

## **Note 8: Restatement**

The Company restated its previously issued consolidated financial statements to correct its error in the application of an accounting principal concerning revenue recognition. Due to substantial uncertainties as to the amount of and timing and collectability of revenues derived from our Physician Managed Model (PMM) and Hybrid Model, which can take in excess of four years to collect, it was determined that these revenues did not meet the criteria for recognition in accordance with ASC 605, Revenue Recognition. These revenues are required to be recorded when collectability is reasonably assured, which in the case of this business model, is when the payment is received and any applicable rapid pay discount offered in the product purchase agreement is applied to the original gross invoice. We have recorded revenues for the three and six months ended June 30, 2012 on this basis and restated revenues for the three months and six months ended June 30, 2011. The effect of the restatement on results of operations and financial position as of and for the three and six months ended June 30, 2011 were as follows:

	<b>As</b>		
	<b>Previously Reported</b>	<b>Restatement Adjustment</b>	<b>Restated</b>
	<b>30-Jun-11</b>		<b>30-Jun-11</b>
Accounts Receivable-Net of Allowance for Doubtful Accounts	\$ 26,545,539	\$ (26,184,050) (1)	\$ 361,489
Allowance for Doubtful Accounts	(771,016)	771,016 (1)	-
Deferred Tax Asset - Short Term	367,489	(238,479) (2)	129,010
Prepaid Taxes	-	167,301 (1)	167,301
<b>Total Current Assets</b>	<b>27,608,283</b>	<b>(25,913,030)</b>	<b>1,695,253</b>
Long-term accounts receivable	2,291,820	(2,291,820) (1)	-
Deferred Tax Asset-Long Term	283,176	1,111,826(2)	1,395,002
<b>Total Assets</b>	<b>33,460,094</b>	<b>(27,093,024)</b>	<b>6,367,070</b>
Taxes Payable	6,666,312	(6,666,312) (2)	-
Deferred Tax Liability - Current	1,288,278	(1,218,630) (2)	69,648
<b>Total Current Liabilities</b>	<b>11,626,935</b>	<b>(7,884,943)</b>	<b>3,741,992</b>
Deferred Income Taxes	2,636,835	(1,848,404) (2)	788,431
<b>Total Liabilities</b>	<b>14,263,770</b>	<b>(9,733,347)</b>	<b>4,530,423</b>
Retained Earnings (Accumulated Deficit)	15,914,928	(17,359,677)	(1,444,749)
<b>Total Shareholders' Equity</b>	<b>19,196,324</b>	<b>(17,359,677)</b>	<b>1,836,647</b>
<b>Total Liabilities and Shareholder Equity</b>	<b>33,460,094</b>	<b>(27,093,024)</b>	<b>6,367,070</b>
<b>Three Months ended</b>	<b>30-Jun-11</b>	<b>Adjustment</b>	<b>30-Jun-11</b>
Product Sales	4,704,619	(2,554,671) (3)	2,149,948
Selling, General and Administrative	2,946,893	(250,000) (4)	2,696,893
Income Taxes	950,023	(950,023) (2)	-
Deferred Income Tax (Benefit)	(368,199)	30,014 (2)	(338,185)
<b>Net Income (Loss)</b>	<b>813,131</b>	<b>(1,384,262)</b>	<b>(571,131)</b>
Comprehensive Income (Loss)	813,131	(1,384,262)	(571,131)
<b>Basic Earnings (Loss) per Share</b>	<b>\$ 0.04</b>	<b>\$ (0.01)</b>	<b>\$ 0.03</b>
<b>Diluted Earnings (Loss) per Share</b>	<b>\$ 0.04</b>	<b>\$ (0.01)</b>	<b>\$ 0.03</b>
<b>Six Months ended</b>	<b>30-Jun-11</b>	<b>Adjustment</b>	<b>30-Jun-11</b>
Product Sales	10,298,054	(6,266,729) (3)	4,031,325
Selling, General and Administrative	5,862,297	(301,436) (4)	5,560,861
Income Taxes	1,647,361	(1,647,361) (2)	-
Deferred Income Tax (Benefit)	(335,149)	(589,011) (2)	(924,160)
<b>Net Income (Loss)</b>	<b>2,228,600</b>	<b>(3,728,921)</b>	<b>(1,500,321)</b>
Comprehensive Income (Loss)	2,225,391	(3,728,921)	(1,503,530)
<b>Basic Earnings (Loss) per Share</b>	<b>\$ 0.10</b>	<b>\$ (0.03)</b>	<b>\$ 0.07</b>
<b>Diluted Earnings (Loss) per Share</b>	<b>\$ 0.10</b>	<b>\$ (0.03)</b>	<b>\$ 0.07</b>

(1) To restate Accounts Receivable and related accounts for the removal of Q2 2011 and historical unrecognized revenues.

(2) To restate Income Taxes to reflect the affect of the change in unrecognized revenues.

(3) To restate Product Sales for the removal of Q2 2011 unrecognized revenues.

(4) To restate Operating Expenses for the removal of Q2 2011 Bad Debt Expense associated with the removal of Q2 2011 unrecognized revenues.

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

This Quarterly Report on Form 10-Q contains forward-looking statements. All statements other than statements of historical fact are, or may be deemed to be, forward-looking statements. Such forward-looking statements include statements regarding, among others, (a) our expectations about possible business combinations, (b) our growth strategies, (c) our future financing plans, and (d) our anticipated needs for working capital. Forward-looking statements, which involve assumptions and describe our future plans, strategies, and expectations, are generally identifiable by use of the words “may,” “will,” “should,” “expect,” “anticipate,” “approximate,” “estimate,” “believe,” “intend,” “plan,” “budget,” “could,” “forecast,” “might,” “predict,” “shall” or “project,” or the negative of these words or other variations on these words or comparable terminology. This information may involve known and unknown risks, uncertainties, and other factors that may cause our actual results, performance, or achievements to be materially different from the future results, performance, or achievements expressed or implied by any forward-looking statements. These statements may be found in this Quarterly Report on Form 10-Q.

Forward-looking statements are based on our current expectations and assumptions regarding our business, potential target businesses, the economy and other future conditions. Because forward-looking statements relate to the future, by their nature, they are subject to inherent uncertainties, risks and changes in circumstances that are difficult to predict. Our actual results may differ materially from those contemplated by the forward-looking statements as a result of various factors, including, without limitation, the risks outlined under “Risk Factors” in our Annual Report on Form 10-K/A, changes in local, regional, national or global political, economic, business, competitive, market (supply and demand) and regulatory conditions and the following:

- Inability to raise sufficient additional capital to operate our business;
- Adverse economic conditions;
- the commercial success and market acceptance of any of our products;
- the maintenance of our products in the FDA National Drug Code database;
- the timing and outcome of clinical studies;
- the outcome of potential future regulatory actions, including inspections from the FDA;
- unexpected regulatory changes, including unanticipated changes to workers compensation state laws and/or regulations;
- the expectation that we will be able to maintain adequate inventories of our commercial products;
- the results of our internal research and development efforts;
- the adequacy of our intellectual property protections and expiration dates on our patents and products;
- the inability to attract and retain qualified senior management and technical personnel;
- the potential impact, if any, of the Patient Protection and Affordable Care Act of 2010 and the Health Care and Education Reconciliation Act of 2010 on our business;
- our plans to develop other product candidates; and
- other specific risks referred to in the section entitled “Risk Factors” in our Annual Report on Form 10-K/A.

We caution you therefore that you should not rely on any of these forward-looking statements as statements of historical fact or as guarantees or assurances of future performance. All forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q. We undertake no obligation to update any forward-looking statements or other information contained herein unless required by law.

### RECENT HIGHLIGHTS OF THE COMPANY UPDATE

- FDA registration of convenience kits in the FDA National Drug Code Database;
- Addition of new distributors and sales representatives;
- Expansion of private insurance market business;
- Publication of the results of controlled clinical trials in peer-reviewed journals;
- Hiring of chief technology officer, medical liaison director and national sales director;
- Expansion of CCPI’s claims submission automation and further upgrades of the *PDRx* software;

**RESULTS OF OPERATIONS  
FOR THE THREE MONTHS ENDED JUNE 30, 2012 AND 2011**

**Three Months ended June 30, 2012 and 2011**

	Three Months June 30,	% of Sales	Three Months June 30, Restated	% of Sales
	2012		2011	
<b>Revenues:</b>				
Product Sales	\$ 1,331,005	91.9%	\$ 2,149,948	90.5%
Service Revenue	117,221	8.1%	224,984	9.5%
<b>Total Revenue</b>	<b>1,448,226</b>	<b>100.0%</b>	<b>2,374,932</b>	<b>100.0%</b>
<b>Cost of Sales:</b>				
Cost of Product Sold	179,678	12.4%	258,273	10.9%
Cost of Services Sold	441,582	30.5%	297,123	12.5%
<b>Total Cost of Sales</b>	<b>621,260</b>	<b>42.9%</b>	<b>555,396</b>	<b>23.4%</b>
<b>Total Gross Profit</b>	<b>826,966</b>	<b>57.1%</b>	<b>1,819,536</b>	<b>76.6%</b>
<b>Operating Expenses:</b>				
Research and Development	30,009	2.1%	32,372	1.4%
Selling, General and Administrative	2,494,018	172.2%	2,696,893	113.6%
<b>Total Operating Expenses</b>	<b>2,524,027</b>	<b>174.3%</b>	<b>2,729,265</b>	<b>115.0%</b>
Net Income (Loss) before Other Income	(1,697,061)	-117.2%	(909,729)	-38.4%
<b>Other Income and Expense</b>				
Interest Income (Expense)	(1,866,818)	-128.9%	-	0.0%
<b>Total Other Income</b>	<b>(1,866,818)</b>	<b>-128.9%</b>	<b>-</b>	<b>0.0%</b>
<b>Net Income (Loss) before Taxes</b>	<b>(3,563,879)</b>	<b>-246.1%</b>	<b>(909,729)</b>	<b>-38.4%</b>
Deferred Income Tax (Benefit)	(739,056)	-51.0%	(338,185)	-14.2%
<b>Net Income (Loss) before Comprehensive Income</b>	<b>(2,824,823)</b>	<b>-195.1%</b>	<b>(571,544)</b>	<b>-24.2%</b>
Unrealized Gain or (Loss) on Investments	-	0.0%	-	0.0%
Reclassification for losses included in Net Income	-	0.0%	-	0.0%
<b>Comprehensive Income (Loss)</b>	<b>\$ (2,824,823)</b>	<b>-195.1%</b>	<b>\$ (571,544)</b>	<b>-24.2%</b>

**Revenue**

Due to substantial uncertainties as to the amount of and timing and collectability of revenues derived from our Physician Managed Model (PMM) and Hybrid Model, which can take in excess of four years to collect, these revenues are recorded when collectability is reasonably assured, which in the case of these two business models, is when the payment is received and any applicable rapid pay discount offered in the product purchase agreement is applied to the original gross invoice. We have recorded revenues for 2012 and 2011 on this basis and restated revenues for the 2010 period. As a result revenues for the two periods are substantially lower than what would have been reported for 2011 and what was reported for 2010. Details of our restatement of previously reported results are included in note number 8 found elsewhere in this report.

Total revenue for the three months ended June 30, 2012 decreased \$926,706, or 39.0%, to \$1,448,226, from the restated amount of \$2,374,932 for the three months ended June 30, 2011. Product revenue decreased \$818,943, or 38.1%, from the restated prior year \$2,149,948 to \$1,331,005, primarily due to decreased collections in our PMM and Hybrid businesses resulting from a decrease in product shipments and claims filed. PMM and Hybrid revenues are based on payments received regardless of when the original invoice and shipment occurred. Product revenue for the respective periods is further described in the following schedule:



## Product Revenues

	Three Months ended				
	Revenue				
	Recognition	June 30,	% of	June 30,	% of
	Basis	2012	Sales	2011	Sales
PMM/Hybrid	cash	807,170	60.6%	1,234,060	57.4%
Direct/Distributor	accrual	523,834	39.4%	952,014	44.3%
Credits			0.0%	(36,126)	-1.7%
Total		<u>1,331,004</u>	<u>100.0%</u>	<u>2,149,948</u>	<u>100.0%</u>

Service revenue decreased \$107,763 or 47.9%, from \$224,984 in the three months ended June 30, 2011 to \$117,221 in the three months ended June 30, 2012 due to a decrease in the billing service fee percentage by CCPI, our billing and claims collection subsidiary and lower collections. Starting with the quarter ended June 30, 2011 we decreased the CCPI fee charged to physician clients from 20 percent to a range of 5 to 10 percent as a courtesy under our billing and collection services.

### *Cost of Products Sold*

The cost of products sold decreased \$78,595, or 30.4%, from \$258,273 in the three months ended June 30, 2011 to \$179,678 in the three months ended June 30, 2012 and the percentage of cost of product sold to product revenue increased from 12.0% for the three months ended June 30, 2011 to 13.5% for the three months ended June 30, 2012. Due to the change in revenue recognition policy costs of products shipped are a period expense while revenue is recognized on payment under our PMM and Hybrid Models .

### *Cost of Services Sold*

The cost of services sold for the three months ended June 30, 2012 increased \$144,459, or 48.6%, from \$297,123 for the three months ended June 30, 2011 to \$441,582 for the three months ended June 30, 2012 and the percentage cost of service sold to service revenue increased from 132.1% to 376.7% in those periods. These costs increased primarily because we increased our collections staff to handle increased billing and collections processing activity and because revenue is not recognized until payments are received. While expenses are recognized in the period incurred, the fee charged by CCPI is recognized upon the collection of the claim on behalf of the physician client, which may occur in future periods. Starting with the quarter ended June 30, 2011 we decreased the CCPI fee charged to physician clients from 20 percent to a range of 5 to 10 percent as a courtesy under our billing and collection services.

### ***Operating Expenses***

Operating expenses for the three months ended June 30, 2012 decreased \$205,238 or 7.5%, to \$2,524,027 from \$2,729,265 for the three months ended June 30, 2011 but increased from 114.9% of revenue to 134.4% of revenue because of higher operating expenses relative to revenue. Operating expenses consist of research and development expense and selling, and general and administrative expenses. Changes in these items are further described below.

### ***Research and Development Expense***

Research and development expenses for the three months ended June 30, 2012 decreased \$2,263, or 7.3%, to \$30,009 from \$32,372 for the three months ended June 30, 2011. The level of expense varies from year to year depending on the number of clinical trials that we have in progress. While we don't currently have any formal ongoing clinical trials or studies in progress, we continue to research new potential products and may engage in future clinical trials or studies.

### ***Selling, General and Administrative Expense***

Selling, general and administrative expense, including salaries, wages and benefits, facility expenses, professional fees, marketing, office expenses, and travel and entertainment expense for the three months ended June 30, 2012 decreased \$202,875 or 7.5 %, to \$2,494,018 from \$2,696,893 for the three months ended June 30, 2011. The decrease in general and administrative expense was primarily due to lower stock-based compensation expense and lower professional fees and costs associated with the filing of our registration statement, associated expenses in connection with becoming a public company , and a decrease in legal fees.

### ***Interest Expense***

Interest expense for the three months ended June 30, 2012 was \$1,866,818 compared with \$0 for the three months ended June 30, 2011. Interest expense includes a non-cash charge of \$1,744,081 for the expensing of all unamortized discount on notes issued to a related party due to the change in the terms of these loans making them payable on demand.

### ***Current and Deferred Income Taxes***

As a result of our assessment that the collection of certain sales could not be reasonably assured at the time of sale, these sales did not meet the criteria of a sale for tax purposes. The Company recalculated its 2010 and 2011 tax liabilities and determined that no income taxes are owed for either year. We have filed amended tax returns for 2010 and intend to file our 2011 returns using a change in accounting method consistent with our financial results restatement. We believe that filing such returns will suspend collection and enforcement efforts by both the IRS and the FTB. We further understand that filing such returns will likely result in tax audits on the part of both agencies. There can be no assurances that the agencies will accept our amended returns and will not pursue collection and enforcement efforts.

We had no current income tax expense for the three months ended June 30, 2012 and June 30, 2011. Deferred income tax benefit for the three months ended June 30, 2012 increased \$400,871 or 118.5 %, to \$739,056 from \$338,185 for the three months ended June 30, 2011.

### ***Net Loss***

Net Loss for the three months ended June 30, 2012 was \$2,824,823 compared to net loss of \$571,531 for the three months ended June 30, 2011. The increased loss was primarily due to lower revenues, partially offset by lower operating expenses and the expensing of unamortized note discount.

**RESULTS OF OPERATIONS  
FOR THE SIX MONTHS ENDED , 2012 AND 2011**

**TARGETED MEDICAL PHARMA, INC.  
CONSOLIDATED STATEMENTS OF INCOME  
Six Months ended June 30, 2012 and 2011**

	Six Months June 30,	% of	Six Months June 30, Restated	% of
	2012	Sales	2011	Sales
<b>Revenues:</b>				
Product Sales	\$ 2,603,815	92.2%	\$ 4,031,325	91.4%
Service Revenue	\$ 219,596	7.8%	\$ 378,932	8.6%
<b>Total Revenue</b>	<b>2,823,411</b>	<b>100.0%</b>	<b>4,410,257</b>	<b>100.0%</b>
<b>Cost of Sales:</b>				
Cost of Product Sold	\$ 369,671	13.1%	\$ 541,933	12.3%
Cost of Services Sold	\$ 886,324	31.4%	\$ 670,462	15.2%
<b>Total Cost of Sales</b>	<b>1,255,995</b>	<b>44.5%</b>	<b>1,212,395</b>	<b>27.5%</b>
<b>Total Gross Profit</b>	<b>1,567,416</b>	<b>55.5%</b>	<b>3,197,862</b>	<b>72.5%</b>
<b>Operating Expenses:</b>				
Research and Development	\$ 57,273	2.0%	\$ 69,120	1.6%
Selling, General and Administrative	\$ 4,778,372	169.2%	\$ 5,560,861	126.1%
<b>Total Operating Expenses</b>	<b>4,835,645</b>	<b>171.2%</b>	<b>5,629,981</b>	<b>127.7%</b>
<b>Net Income (Loss) before Other Income</b>	<b>(3,268,229)</b>	<b>-115.7%</b>	<b>(2,432,119)</b>	<b>-20.6%</b>
<b>Other Income and Expense</b>				
Interest Income (Expense)	(1,942,657)	-68.8%	-	0.0%
Investment Income	-	0.0%	7,638	0.2%
<b>Total Other Income</b>	<b>(1,942,657)</b>	<b>-68.8%</b>	<b>7,638</b>	<b>0.2%</b>
<b>Net Income (Loss) before Taxes</b>	<b>(5,210,886)</b>	<b>-184.5%</b>	<b>(2,424,481)</b>	<b>-55.0%</b>
Deferred Income Tax (Benefit)	(1,410,146)	-49.9%	(924,160)	-21.0%
<b>Net Income (Loss) before Comprehensive Income</b>	<b>(3,800,740)</b>	<b>-134.6%</b>	<b>(1,500,321)</b>	<b>-34.0%</b>
Unrealized Gain or (Loss) on Investments	-	0.0%	-	0.0%
Reclassification for losses included in Net Income	-	0.0%	(3,209)	-0.1%
<b>Comprehensive Income (Loss)</b>	<b>\$ (3,800,740)</b>	<b>-134.6%</b>	<b>\$ (1,503,530)</b>	<b>-34.1%</b>

**Revenue**

Due to substantial uncertainties as to the amount of and timing and collectability of revenues derived from our Physician Managed Model (PMM) and Hybrid Model, which can take in excess of four years to collect, these revenues are recorded when collectability is reasonably assured, which in the case of these two business models, is when the payment is received and any applicable rapid pay discount offered in the product purchase agreement is applied to the original gross invoice. We have recorded revenues for 2012 and 2011 on this basis and restated revenues for the quarterly periods in 2011 and the 2010 annual period. As a result revenues for the two periods are substantially lower that what would have been reported for 2011 and what was reported for 2010. Details of our restatement of previously reported results are included in note number 8 found elsewhere in this report.

Total revenue for the six months ended June 30, 2012 decreased \$1,586,846, or 36.0%, to \$2,823,411, from the restated amount of \$4,410,257 for the six months ended June 30, 2011. Product revenue decreased \$1,427,510, or 35.4%, from the restated prior year \$4,031,325 to \$2,603,815, primarily due to decreased collections in our PMM and Hybrid businesses resulting from reduced product shipments and fewer claims filed. PMM and Hybrid revenues are based on payments received regardless of when the original invoice and shipment occurred. Product revenue for the respective periods is further described in the following schedule:

<b>Six Months ended</b>					
<b>Revenue</b>					
<b>Recognition</b>		<b>June 30,</b>	<b>% of</b>	<b>June 30,</b>	<b>% of</b>
<b>Basis</b>		<b>2012</b>	<b>Sales</b>	<b>2011</b>	<b>Sales</b>
PMM/Hybrid	cash	1,570,915	60.3%	2,183,079	54.2%
Direct/Distributor	accrual	1,042,115	40.0%	1,914,264	47.5%
Credits		(9,216)	-0.4%	(66,017)	-1.6%
Total		<u>2,603,814</u>	<u>100.0%</u>	<u>4,031,326</u>	<u>100.0%</u>

Service revenue decreased \$159,336 or 42.0%, from \$378,932 in the six months ended June 30, 2011 to \$219,596 in the six months ended June 30, 2012 due to a decrease in the billing service fee percentage by CCPI, our billing and claims collection subsidiary. Starting with the quarter ended , 2011 we decreased the CCPI fee charged to physician clients from 20 percent to a range of 5 to 10 percent as a courtesy under our billing and collection services.

#### ***Cost of Products Sold***

The cost of products sold decreased \$172,262, or 31.8%, from \$541,933 in the six months ended June 30, 2011 to \$369,671 in the six months ended June 30, 2012 and the percentage of cost of product sold to product revenue increased from 13.4% for the six months ended June 30, 2011 to 14.2% for the six months ended June 30, 2012. Due to the change in revenue recognition policy costs of products shipped are a period expense while revenue is recognized on payment under our PMM and Hybrid .

#### ***Cost of Services Sold***

The cost of services sold for the six months ended June 30, 2012 increased \$215,862, or 32.2%, from \$670,462 for the six months ended June 30, 2011 to \$886,324 for the six months ended June 30, 2012 and the percentage cost of service sold to service revenue increased from 176.9% to 403.6% in those periods due to higher costs and lower collections. These costs increased primarily because we increased our collections staff to handle increased billing and collections processing activity. While expenses are recognized in the period incurred, our fee is recognized upon the collection of the claim on behalf of the physician client, which may occur in future periods. Starting with the quarter ended , 2011 we decreased the CCPI fee charged to physician clients from 20 percent to a range of 5 to 10 percent as a courtesy under our billing and collection services.

### ***Operating Expenses***

Operating expenses for the six months ended June 30, 2012 decreased \$794,336 or 14.1%, to \$4,835,645 from \$5,629,981 for the six months ended June 30, 2011 but increased from 127.7% of revenue to 134.4% of revenue because of the higher expense in relation to revenue. Operating expenses consist of research and development expense and selling, and general and administrative expenses. Changes in these items are further described below.

### ***Research and Development Expense***

Research and development expenses for the six months ended June 30, 2012 decreased \$11,847, or 17.1%, to \$57,273 from \$69,120 for the six months ended June 30, 2011. The level of expense varies from year to year depending on the number of clinical trials that we have in progress. While we don't currently have any formal ongoing clinical trials or studies in progress, we continue to research new potential products and may engage in future clinical trials or studies.

### ***Selling, General and Administrative Expense***

Selling, general and administrative expense, including salaries, wages and benefits, facility expenses, professional fees, marketing, office expenses, and travel and entertainment expense for the six months ended June 30, 2012 decreased \$782,480 or 14.1%, to \$4,778,372 from \$5,560,861 for the six months ended June 30, 2011. The decrease in general and administrative expense was primarily due to lower stock-based compensation expense and lower professional fees and costs associated with the filing of our registration statement, associated expenses in connection with becoming a public company, and a decrease in legal fees.

### ***Interest Expense***

Interest expense for the six months ended June 30, 2012 was \$1,942,657 compared with \$0 for the six months ended June 30, 2011. Interest expense includes a non-cash charge of \$1,744,081 for the expensing of all unamortized discount on notes issued to a related party due to the change in the terms of these loans making them payable on demand.

### ***Current and Deferred Income Taxes***

As a result of our assessment that for certain sales' collectability at the time of the sale could not be reasonably assured, these sales did not meet the criteria of a sale for tax purposes. The Company recalculated its 2010 and 2011 tax liabilities and determined that no income taxes are owed for either year. We filed amended tax returns for 2010 and intend to file our 2011 returns using a change in accounting method consistent with our financial results restatement. We believe that filing such returns will suspend collection and enforcement efforts by both the IRS and the FTB. We further understand that filing such returns will likely result in tax audits on the part of both agencies. There can be no assurances that the agencies will accept our amended returns and will not pursue collection and enforcement efforts.

We had no current income tax expense for the six months ended June 30, 2012 and June 30, 2011. Deferred income tax benefit for the six months ended June 30, 2012 increased \$485,986 or 52.6 %, to \$1,410,146 from \$924,160 for the six months ended June 30, 2011.

### ***Net Loss***

Net Loss for the six months ended June 30, 2012 was \$3,800,740 compared to net loss of \$1,503,530 for the six months ended June 30, 2011. The increased loss was primarily due to lower revenues, partially offset by lower operating expenses and the expensing of unamortized note discount.

### **FINANCIAL CONDITION**

Our negative working capital of \$8,060,392 as of June 30, 2012, increased by \$3,476,816 from our December 31, 2011 working capital of \$4,583,576. The larger negative balance was primarily due to the increase in notes payable to related parties and accounts payable and accrued expenses. Inventory increased by \$644,814, partially due to an advanced purchase for a pending contract. Notes payable to related parties by \$2,885,000 during the six months ended June 30, 2012, and accounts payable and accrued expenses increased by \$861,902.

### ***Accounts Receivable***

As a result of our change in revenue recognition policy, as of June 30, 2012 we have \$33,800,000 in unrecorded revenues that potentially will be recorded as revenue by TMP in the future as our CCPI subsidiary secures claims payments on behalf of our PMM and Hybrid Customers. Except for collection expenses incurred by CCPI in future periods, all expenses associated with these unrecorded revenues including cost of products sold have already been reflected in our financial statements. In addition, due to loss carry forwards we should not incur current tax liabilities for a substantial portion of these unrecorded revenues.

## LIQUIDITY AND CAPITAL RESOURCES

We have historically financed operations through cash flows from operations as well as equity transactions and related party loans. As of June 30, 2012 our principal source of liquidity was \$44,603 in cash and cash and potential related party loans. Due to the uncertainty of our ability to meet our current operating and capital expenses, in their report on our audited annual financial statements as of and for the years ended December 31, 2011 and 2010, our independent auditors included an explanatory paragraph regarding concerns about our ability to continue as a going concern. Our consolidated financial statements contain additional note disclosures describing the circumstances that led to this disclosure by our independent auditors. There is substantial doubt about our ability to continue as a going concern as the continuation and expansion of our business is dependent upon obtaining further financing, development of revenue streams with shorter collection times and accelerating collections on our physician managed and hybrid revenue streams.

The Company continues to experience negative operating cash flow. Since July 1, 2011 the Company has supplemented the funding of its operations through borrowings from a related party, the Elizabeth Charuvastra and William Shell Family Trust. Through August 14, 2012 these loans total \$4,327,000 of which \$3,175,000 have occurred since January 1, 2012. The Company continues to pursue additional sources of liquidity including asset-based loans and selective sale of some of the \$33.8 million in invoices payable to the Company by our physician and distributor customers. We may also consider raising money through an equity transaction. Until and unless these efforts prove successful the Company will continue to rely on related party loans as a supplemental source of liquidity. There can be no assurance that future financing can be obtained on terms acceptable to the Company.

Through December 31, 2009, we reported income to the Internal Revenue Service on the cash basis. Beginning with the year ended December 31, 2010, we reported our taxable income on the accrual basis as of, for the quarter ended December 31, 2010; we surpassed the gross receipts threshold set in the Internal Revenue Code of 1986, as amended, which requires a switch from cash to accrual method. The impact of this change in reporting method is that more income taxes are current under the accrual method compared to deferred under the cash method.

The Company filed its 2010 federal and state tax returns in April 2011 and June 2011, respectively, and did not pay the amounts stated and due. As of the date of this 10-Q, without taking into effect the expected filing of amendments to the tax returns to reflect the affects of the restatements noted below and elsewhere in this 10-Q, the Company would owe \$3,592,828 in federal taxes and \$946,582 in state taxes in respect of our 2010 tax returns. The Company subsequently entered into payment agreements with the Internal Revenue Service (the "IRS") and the California Franchise Tax Board (the "CFTB") but was unable to meet the terms of either plan. As a result of our failure to pay taxes due and to make all agreed-upon installment payments, the IRS filed a general lien against the Company on February 17, 2012. The IRS proposed monthly payments of \$150,000 beginning on March 28, 2012 in order to avoid enforcement action against the Company. We failed to make a payment to the IRS on March 28, 2012 and have made no further payments to the IRS. The CFTB filed a "Final Notice Before Suspension/Forfeiture" on March 23, 2012 effective June 1, 2012, however the CFTB has not filed a lien against the Company and agreed to forestall action if the Company made monthly payments of \$100,000 beginning on April 20, 2012. The Company made such payment. As a result of the restatement of our financial statements, which showed significantly reduced revenue for 2010, we filed amended federal and state tax returns showing that we have no liability for unpaid taxes to the IRS and CFTB. Since the filing of these returns amended tax returns, the collection and enforcement efforts by the IRS and CFTB have been suspended. These amended returns may result in protracted audits of the Company and there can be no assurance that either the IRS or the CFTB will accept our amendments or restart their collection and enforcement efforts. We have not received any notices regarding the status of the review of our amended tax returns. Until these returns are reviewed and resolved we will request and expect to receive further extension of the collection and enforcement efforts suspensions. We will also be filing our 2011 income returns by the relevant extended filing deadlines in September and October 2012.

Net cash used by operating activities for the six months ended June 30, 2012 was \$2,759,083 compared to \$919,008 cash used by operating activities for the six months ended June 30, 2011.

Net cash used by investing activities was \$323,233 for the six months ended June 30, 2011 and \$194,616 cash used by investing activities for the six months ended June 30, 2012. During the six months ended June 30, 2012 and 2011, we incurred internal software development costs for our *PDRx* claims management and collection system of \$165,810 and \$369,172, respectively and purchased property and equipment of \$157,423 and \$66,651 respectively. Historically, capital expenditures have been financed by cash from operating activities and related party loans. We sold \$241,207 of investments in the six months ended June 30, 2011.

During the six months ended June 30, 2012, we have received \$2,885,000 in exchange for promissory notes issued to the EC and WS Family Trust of which Dr. Shell, our Chief Executive Officer is a trustee. Details of these loans are discussed above in Note 4.

## OFF-BALANCE SHEET ARRANGEMENTS

We have no off-balance sheet arrangements that have a material current effect, or that are reasonably likely to have a material future effect, on our financial condition, changes in financial condition, revenue or expenses, results of operations, liquidity, capital expenditures, or capital resources.

## CONTRACTUAL OBLIGATIONS

The Company leases its operating facility under a lease agreement expiring February 28, 2015 at the rate of \$13,183 per month and several smaller storage spaces rented on a month-to-month basis. The Company, as lessee, is required to pay for all insurance, repairs and maintenance and any increases in real property taxes over the lease period on the operating facility.

## CRITICAL ACCOUNTING POLICIES

### *Principles of consolidation*

The consolidated financial statements include accounts of TMP and its wholly owned subsidiary, CCPI, collectively referred to as “the Company”. All significant intercompany accounts and transactions have been eliminated in consolidation. In addition, TMP and CCPI share the common operating facility, certain employees and various costs. Such expenses are principally paid by TMP. Due to the nature of the parent and subsidiaries relationship, the individual financial position and operating results of TMP and CCPI may be different from those that would have been obtained if they were autonomous.

### *Accounting estimates*

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### *Revenue Recognition*

Under the following revenue models product sales are invoiced upon shipment:

- *Physician Direct Sales Model* (1% of revenue for the six months ended June 30, 2012): Under this model, a physician purchases products from TMP but does not retain CCPI’s services. TMP invoices the physician upon shipment under terms which allow a significant rapid pay discount off AWP for payment within discount terms in accordance with the product purchase agreement. The physicians dispense the product and perform their own claims processing and collections. TMP recognizes revenue under this model on the date of shipment at the gross invoice amount less the anticipated rapid pay discount offered in the product purchase agreement. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% may be applied to the outstanding balance. The physician is responsible for payment directly to TMP.
- *Distributor Direct Sales Model* (36% of revenue for the six months ended June 30, 2012): Under this model, a distributor purchases products from TMP and sells those products to a physician and the physician does not retain CCPI’s services. TMP invoices distributors upon shipment under terms which include a significant discount off AWP. TMP recognizes revenue under this model on the date of shipment at the net invoice amount. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% may be applied to the outstanding balance.

Due to substantial uncertainties as to the timing and collectability of revenues derived from our Physician Managed and Hybrid models described below, which can take in excess of four years to collect, we have determined that these revenues did not meet the criteria for recognition in accordance with ASC 605, *Revenue Recognition*. These revenues are therefore required to be recorded when collectability is reasonably assured, which the Company has determined is when the payment is received.

- *Physician Managed Model* (45% of revenue for the six months ended June 30, 2012): Under this model, a physician purchases products from TMP and retains CCPI’s services. TMP invoices physician upon shipment to physician under terms which allow a significant rapid pay discount for payment received within terms in accordance with the product purchase agreement which includes a security interest for TMP in the products and receivables generated by the dispensing of the products. The physician also executes a billing and claims processing services agreement with CCPI for billing and collection services relating to our products (discussed below). CCPI submits a claim for reimbursement on behalf of the physician client. The CCPI fee and product invoice amount are deducted from the reimbursement received by CCPI on behalf of the physician client before the reimbursement is forwarded to the physician client. In the event the physician fails to pay the product invoice within the agreed term, we can deduct the payment due from any of the reimbursements received by us on behalf of the physician client as a result of the security interest we obtained in the products we sold to the physician client and the receivables generated by selling the products in accordance with our agreement. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% is applied to the outstanding balance. However, since we are in the early stage of our business, as a courtesy to our physician clients, our general practice has been to extend the rapid pay discount beyond the initial term of the invoice until the invoice is paid and not to apply a late payment fee to the outstanding balance. TMP recognizes revenue under this model on the date payment is received at the gross invoice amount less the applicable rapid pay discount offered in the product purchase agreement





- *Hybrid Model* (11% of revenue for the six months ended June 30, 2012): Under this model, a distributor purchase products from TMP and sell those products to a physician and the physician retains CCPI's services. TMP invoices distributors upon shipment under terms which allow a significant rapid pay discount for payment received within terms in accordance with the product purchase agreements. The physician client of the distributor executes a billing and claims processing services agreement with CCPI for billing and collection services (discussed below). The distributor product invoice and the CCPI fee are deducted from the reimbursement received by CCPI on behalf of the physician client before the reimbursement is forwarded to the distributor for further delivery to their physician clients. In the event payment is not received within the term of the agreement, the amount payable for the purchased TMP products reverts to the AWP. In addition, if payment is not received within the agreed-upon term, a late payment fee of up to 20% is applied to the outstanding balance. However, since we are in the early stage of our business, as a courtesy to our physician clients, our general practice has been to extend the rapid pay discount beyond the initial term of the invoice until the invoice is paid and not to apply a late payment fee to the outstanding balance. TMP recognizes revenue under this model on the date payment is received at the net invoice amount.

### ***Allowance for doubtful accounts***

Under the direct sales to physician and direct sales to distributor models, product is sold under terms that allow substantial discounts (40-88%) for payment within terms. With such substantial discounts, it is rare that an invoice is not paid within terms. We have not experienced any write offs associated with these revenue models.

Under the Company's physician managed model and hybrid model, CCPI performs billing and collection services on behalf of the physician client and deducts the CCPI fee and product invoice amount from the reimbursement received by CCPI on behalf of the physician client before the reimbursement is forwarded to the physician client. Extended collection periods are typical in the workers compensation industry with payment terms extending from 45 days to in excess of four years. The physician remains personally liable for purchases of product from TMP and, during this long collection cycle, TMP retains a security interest in all products sold to the physician along with the claims receivable that result from sales of the products. CCPI maintains an accounting of all managed accounts receivable on behalf of the physician and regularly reports to the physician. As described above, due to uncertainties as to the timing and collectability of revenues derived from these models, revenue is recorded when payment is received therefore no allowance for doubtful accounts is necessary.

In addition to the bad debt recognition policy above, it is also TMP's policy to write down uncollectible loans and trade receivables when the payer is no longer in existence, is in bankruptcy or is otherwise insolvent. In such instances our policy is to reduce accounts receivable by the uncollectible amount and to proportionally reduce the allowance for doubtful accounts.

### ***Inventory valuation***

Inventory is valued at the lower of cost (first in, first out) or market and consists primarily of finished goods.

### ***Impairment of long-lived assets***

The long-lived assets held and used by the Company are reviewed for impairment no less frequently than annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In the event that facts and circumstances indicate that the cost of any long-lived assets may be impaired, an evaluation of recoverability is performed. No asset impairment was recorded at June 30, 2012 or at June 30, 2011.

### ***Intangible assets***

Indefinite lived intangible assets are measured for impairment at least annually, and more often when events indicate that an impairment may exist. Intangible assets with finite lives, including patents and internally developed software (primarily the Company's PDRx system), are stated at cost and are amortized over their useful lives. Patents are amortized on a straight line basis over their statutory lives, usually fifteen to twenty years. Internally developed software is amortized over three to five years. Intangible assets with indefinite lives are tested annually for impairment, during the fiscal fourth quarter and between annual periods, if impairment indicators exist, and are written down to fair value as required.

### ***Fair value of financial instruments:***

The Company's financial instruments are accounts receivable and accounts payable. The recorded values of accounts receivable and accounts payable approximate their values based on their short term nature.

### ***Income taxes***

The Company determines its income taxes under the asset and liability method. Under the asset and liability approach, deferred income tax assets and liabilities are calculated and recorded based upon the future tax consequences of temporary differences by applying enacted statutory tax rates applicable to future periods for differences between the financial statements carrying amounts and the tax basis of existing assets and liabilities. Generally, deferred income taxes are classified as current or non-current in accordance with the classification of the related asset or liability. Those not related to an asset or liability are classified as current or non-current depending on the periods in which the temporary differences are expected to reverse. Valuation allowances are provided for significant deferred income tax assets when it is more likely than not that some or all of the deferred tax assets will not be realized.

The Company recognizes tax liabilities by prescribing a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized, and also provides guidance on de-recognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. The minimum threshold is defined as a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. To the extent that the final tax outcome of these matters is different than the amount recorded, such differences impact income tax expense in the period in which such determination is made. Interest and penalties, if any, related to accrued liabilities for potential tax assessments are included in income tax expense.

### ***Stock-Based Compensation***

The Company accounts for stock option awards in accordance with ASC 718. Under ASC 718, compensation expense related to stock-based payments is recorded over the requisite service period based on the grant date fair value of the awards. Compensation previously recorded for unvested stock options that are forfeited is reversed upon forfeiture. The Company uses the Black-Scholes option pricing model for determining the estimated fair value for stock-based awards. The Black-Scholes model requires the use of assumptions which determine the fair value of stock-based awards, including the option's expected term and the price volatility of the underlying stock.

The Company's accounting policy for equity instruments issued to consultants and vendors in exchange for goods and services follows the provisions of ASC 505-50. Accordingly, the measurement date for the fair value of the equity instruments issued is determined at the earlier of (i) the date at which a commitment for performance by the consultant or vendor is reached or (ii) the date at which the consultant or vendor's performance is complete. In the case of equity instruments issued to consultants, the fair value of the equity instrument is recognized over the term of the consulting agreement. Stock-based compensation is a non-cash expense because we settle these obligations by issuing shares of our common stock from our authorized shares instead of settling such obligations with cash payments.

### ***Earnings Per Share***

The Company utilizes FASB ASC 260, "Earnings per Share". Basic income (loss) per share is computed by dividing income (loss) available to common shareholders by the weighted-average number of common shares outstanding. Diluted income (loss) per share is computed similar to basic income (loss) per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. Common equivalent shares are excluded from the computation if their effect is anti-dilutive.

The following potential common shares have been excluded from the computation of diluted net income (loss) per share for the periods presented where the effect would have been anti-dilutive:

At June 30,	2012	2011
Options outstanding	1,893,444	291,347

### ***Research and development***

Research and development costs are expensed as incurred. In instances where we enter into agreements with third parties for research and development activities on our behalf, we may prepay fees for services at the initiation of the contract. We record the prepayment as a prepaid asset and amortize the asset into research and development expense over the period of time the contracted research and development services are performed. Most contract research agreements include a ten year records retention and maintenance requirement. Typically, we expense 50% of the contract amount upon completion of the clinical trials and 50% over the remainder of the record retention requirements under the contract research organization contract.

### **Item 3. Quantitative and Qualitative Disclosure About Market Risk**

We are a smaller reporting company and therefore, we are not required to provide information required by this Item.

### **Item 4. Controls and Procedures**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that (a) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (b) provide reasonable assurance that transactions are recorded as necessary to permit the preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the Company are being made only in accordance with authorizations of the our management and directors; and (c) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements. Based on our evaluation under the framework in Internal Control—Integrated Framework, our management concluded that our internal control over financial reporting was not effective as of June 30, 2012.

In light of the material weaknesses described below, additional analyses and other procedures were performed to ensure that the Company's condensed consolidated financial statements included in this Quarterly Report on Form 10-Q were prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP"). These measures included expanded quarter-end closing procedures, the dedication of significant internal resources to scrutinize account analyses and reconciliations, and management's own internal reviews and efforts to remediate the material weaknesses in internal control over financial reporting described below.

#### **Changes in Internal Controls over Financial Reporting**

Except as described below with respect to the Company's restatement of its financial statements, there were no changes in the Company's internal control over financial reporting during the quarter ended June 30, 2012 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

#### **In-Process Remediation Actions to Address the Internal Controls Weaknesses**

Management identified the following material weaknesses in the Company's internal control over financial reporting as of December 31, 2011, which continue to exist as of June 30, 2012:

- 1) Control activities related to accounting discipline:** There was a certain lack of review and reconciliation in many areas of the accounting function.
- 2) Control activities related to accounts receivable:** PTL accounts receivable subsidiary ledger does not reconcile with the general ledger.
- 3) Control activities related to accounts receivable:** We identified deficiencies regarding accounts receivable subsidiary ledgers of managed physician accounts in CCPI.
- 4) Control activities related to internally developed software:** Generally accepted accounting principles identify four stages of internally developed software. Costs are to be either expensed or capitalized based on their classification within these stages. We were currently capitalizing and depreciating all costs related to internally developed software.

The material weakness in the Company's internal control over financial reporting as of December 31, 2011 for the incorrect application of the accounting principal concerning revenue recognition was remedied when the Company restated its previously issued consolidated financial statements for the fiscal year ended 2010 to correct this error and prepared the fiscal year ended 2011 financial statements using the correct revenue recognition basis. The correct revenue recognition basis has also been applied consistently in fiscal 2012 and the Company intends to restate its interim financial statements for 2011.

In response to the identified material weaknesses described above, the Company is working on improving its control activities. Management believes that actions taken during the quarter ended June 30, 2012, along with other improvements not yet implemented, will address the material weaknesses in the Company's internal control over financial reporting described above. Company management plans to continue to review and make changes to the overall design of its control environment, including the roles and responsibilities within the organization and reporting structure, as well as policies and procedures to improve the overall internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 1. Legal Proceedings.**

None.

### **Item 1A. Risk Factors.**

We are a smaller reporting company and therefore, we are not required to provide information required by this Item.

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

None.

### **Item 3. Defaults Upon Senior Securities.**

None.

### **Item 4. Mine Safety Disclosures.**

Not applicable.

### **Item 5. Other Information**

Effective July 20, 2012, the Company and AFH Holding and Advisory, LLC (“AFH Advisory”) entered into a letter agreement (the “Letter Agreement”) which was supplemented July 25, 2012 which details the parties agreement and supersedes all earlier agreements between the parties. The parties agreed as follows:

1. **Form 211.** “AFH Advisory” shall assist and advise the Company and its affiliates in facilitating the quotation of the Company’s shares of common stock on the OTC Bulletin Board by identifying and helping the Company to engage the necessary market maker to file a Form 211, or 15c2-11 Exemption Form as applicable, with the Financial Industry Regulatory Authority (“FINRA”).
2. **No Share Forfeiture and Continuing Registration Rights.** AFH Advisory has, and shall continue to have, normal and customary piggyback registration rights with respect to its shares of common stock, as further set forth in the Registration Rights Agreement, dated January 31, 2011. AFH Advisory and its affiliates will no longer be required to forfeit shares as a result of the failure to complete a financing.
3. **Reimbursement of Costs.** AFH Advisory is entitled to a reimbursement of \$585,448 of expenses incurred on behalf of the Company in connection with the Business Combination, and related matters (the “Expense Reimbursement Amount”). Concurrently with the execution of this New Agreement, the Company shall issue to AFH Advisory a Secured Convertible Promissory Note in the principal amount equal to the Expense Reimbursement Amount with interest payable quarterly in arrears at a rate of 8.5% per annum. A Security Agreement was also entered into with AFH effective July 20, 2012 assigning certain assets of the Company to AGH as collateral for the Promissory Note. The \$585,448 may be offset by \$250,000 or any remaining portion thereof relating to payments advanced to AFH Advisory by the Company in connection with a contemplated asset-based loan.
4. **Warrants.** In partial consideration for its services in connection with the Business Combination, upon the approval of the Company’s Board of Directors, the Company shall issue to AFH Advisory five-year warrants to purchase 1,063,981 shares of common stock of the Company (the “Warrant Stock”), at an exercise price of \$1.00 per share. If and whenever the Company shall either (i) reduce, or be deemed to have reduced, the exercise price or conversion price of any of its outstanding warrants to purchase shares of Common Stock of the Company, or any other security exercisable for, or convertible into, shares of Common Stock of the Company, to a price lower than the Exercise Price of the Warrant in effect immediately prior to the time of such reduction, or (ii) issues or sells, or is deemed to have issued or sold, any additional warrants to purchase shares of Common Stock of the Company, or any other security exercisable for, or convertible into, shares of Common Stock of the Company, with a price lower than the Exercise Price of the Warrant in effect immediately prior to the time of such issuance or sale, then, and in each such case, the then-existing Exercise Price of the Warrant shall be reduced to a price equal to the exercise price or conversion price of such amended or newly-issued or sold security.
5. **Board Oversight.** For a period of two (2) years following the date hereof, AFH Advisory shall have a right to disapprove two nominees for director chosen by the board of directors.
6. **Advisory Role.** For a period of two (2) years from the date of this letter agreement, AFH Advisory has the non-exclusive right to act as advisor to the Company on any proposed financings and/or mergers and acquisitions, to be separately engaged on a deal by deal basis at the Company’s discretion with respect to any specific transaction, the Company may choose not to retain AFH and Advisory as an advisor.

On August 13, 2012, the Company, AFH Advisory, Dr. Shell, the Estate of Elizabeth Charuvastra (the “Estate”), our former Chairman and Vice President of Regulatory Affairs, and Mr. Giffoni (collectively Dr. Shell, the Estate and Mr. Giffoni, the “Insiders”) entered into Amendment No. 2 (“Amendment No. 2”) to the Agreement and Plan of Reorganization. Pursuant to Amendment No. 2, the make good provision, pursuant to which the Insiders

had agreed to cancel up to 1,906,768 shares in the aggregate in the event stated EBITDA targeted were not achieved by the Company, has been deleted in its entirety.

**Item 6. Exhibits.**

<b>Number</b>	<b>Description</b>
10.1	Letter Agreement, dated July 20, 2012, by and between Targeted Medical Pharma, Inc. and AFH Advisory and Holdings, LLC
10.2	Letter Supplement, dated July 25, 2012 by and between Targeted Medical Pharma, Inc. and AFH Advisory and Holdings, LLC
10.3	Amendment 2 to Agreement and Plan of Reorganization, dated August 13, 2012, by and between Targeted Medical Pharma, Inc., AFH Advisory and Holdings, LLC, William E. Shell, MD, the Estate of Elizabeth Charuvastra and Kim Giffoni
10.4	Secured Convertible Promissory Note, dated July 20, 2012, issued by Targeted Medical Pharma, Inc. in favor of AFH Holding and Advisory, LLC
10.5	Security Agreement, dated July 20, 2012, by and between Targeted Medical Pharma, Inc. and AFH Holding and Advisory, LLC
31.1	Certification of Chief Executive Officer Pursuant To Sarbanes-Oxley Section 302
31.2	Certification of Chief Financial Officer Pursuant To Sarbanes-Oxley Section 302
32.1*	Certification Pursuant To 18 U.S.C. Section 1350
101.ins**	XBRL Instance Document
101.xsd**	XBRL Taxonomy Extension Schema Document
101.cal**	XBRL Taxonomy Calculation Linkbase Document
101.def**	XBRL Taxonomy Definition Linkbase Document
101.lab**	XBRL Taxonomy Label Linkbase Document
101.pre**	XBRL Taxonomy Presentation Linkbase Document

\* Furnished. Not filed. Not incorporated by reference. Not subject to liability.

\*\* A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized on the 14th day of August, 2012.

### TARGETED MEDICAL PHARMA, INC.

By: /s/ William E. Shell, MD  
William E. Shell, MD  
Chief Executive Officer

By: /s/ Ronald W. Rudolph  
Ronald W. Rudolph  
Chief Financial Officer



## EXHIBIT INDEX

<b>Number</b>	<b>Description</b>
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31.1	Certification of Chief Executive Officer Pursuant To Sarbanes-Oxley Section 302
31.2	Certification of Interim Chief Financial Officer Pursuant To Sarbanes-Oxley Section 302
32.1	Certification Pursuant To 18 U.S.C. Section 1350 (*)
101.ins*	XBRL Instance Document
101.xsd*	XBRL Taxonomy Extension Schema Document
101.cal*	XBRL Taxonomy Calculation Linkbase Document
101.def*	XBRL Taxonomy Definition Linkbase Document
101.lab*	XBRL Taxonomy Label Linkbase Document
101.pre*	XBRL Taxonomy Presentation Linkbase Document

\*Furnished. Not filed. Not incorporated by reference. Not subject to liability.

Targeted Medical Pharma, Inc.  
2980 Beverly Glen Circle  
Suite 301  
Los Angeles, California 9077

July 20, 2012

AFH Holding and Advisory, LLC  
9595 Wilshire Boulevard  
Suite 700  
Beverly Hills, California 90212

Gentlemen:

Reference is hereby made to the Letter of Intent, dated January 25, 2011, by and between Targeted Medical Pharma, Inc. (“the Company”) and AFH Holding and Advisory, LLC (“AFH Advisory”), as amended on October 6, 2011 (the “Letter of Intent”) (Except as otherwise set forth herein, capitalized terms used and not otherwise defined herein are used as defined in the Letter of Intent). Pursuant to the Letter of Intent, among other things, the Business Combination was consummated, and the Business Combination Shares were issued, as of January 31, 2011. The parties acknowledge and agree that the Offering, and certain related transactions, contemplated by the Letter of Intent have not been consummated, and the registration statement relating to the Offering, which was filed with the Securities and Exchange Commission on February 14, 2011, has been withdrawn by the Company. The parties desire to set forth their agreement with respect to the outstanding obligations under the Letter of Intent, and related matters and, in accordance therewith, this agreement (the “New Agreement”) supersedes the Letter of Intent in its entirety and sets forth the revised agreement of the signatories hereto, as follows:

1. **Form 211.** AFH Holding and Advisory LLC (“AFH Advisory”) shall assist and advise the Company and its affiliates in facilitating the quotation of the Company’s shares of common stock on the OTC Bulletin Board by identifying and helping the Company to engage the necessary market maker to file a Form 211, or 15c2-11 Exemption Form, as applicable, with the Financial Industry Regulatory Authority (the “Form 211 Filing”).
  2. **Registration Rights.** AFH Advisory has, and shall continue to have, normal and customary piggyback registration rights with respect to the Advisor Shares, as further set forth in the Registration Rights Agreement, dated January 31, 2011, which was entered into in connection with the Business Combination. Further, the parties acknowledge that the Advisor Shares are currently eligible for resale pursuant to Rule 144 under the Securities Act of 1933, as amended (“Rule 144”), and the Company agrees to use its best efforts to assist AFH Advisory in effecting any sales of the Advisor Shares pursuant to Rule 144, or other available exemption under the Securities Act of 1933, including without limitation, by delivering an opinion of counsel to the Company’s transfer agent in form, substance and scope customary for opinions of counsel in comparable transactions.
-

- 3. Reimbursement of Costs.** AFH Advisory is entitled to a reimbursement of \$585,448 of expenses incurred on behalf of the Company in connection with the Business Combination, and related matters (the “Expense Reimbursement Amount”). Concurrently with the execution of this New Agreement, the Company shall issue to AFH Advisory a Secured Convertible Promissory Note in the principal amount equal to the Expense Reimbursement Amount, with interest payable quarterly in arrears at a rate of 8.5% per annum, in substantially the form attached hereto as Exhibit A (the “Note”), pursuant to which, among other things: (a) AFH Advisory shall be entitled, in its sole discretion, to either be repaid any amounts due under the Note in cash, or to convert such amounts, or any portion thereof, into additional shares of common stock of the Company (“Conversion Shares”) at the Conversion Price (as defined in the Note) as further set forth in Section 2.1 of the Note, (b) AFH Advisory may, in its sole discretion, elect to be repaid any amounts due under the Note out of the proceeds of any financings completed by the Company, as further set forth Section 1.2 of the Note, (c) AFH Advisory shall have normal and customary piggyback registration rights with respect to the Conversion Shares, as further set forth in Sections 6.1 through 6.3 of the Note , (d) the principal amount of the Note shall be reduced by an amount equal to the difference between the \$250,000 the Company previously advanced to AFH Advisory in connection with the Receivables Transaction (as defined in the Note) and the amount of expenses actually incurred in connection with such Receivables Transaction, as further set forth in Section 1.3 of the Note, and (e) all obligations of the Company under the Note are secured by a security interest in and to certain assets of the Company, as further set forth in Section 3.1 of the Note, and in the Security Agreement by and between the parties, dated of even date herewith, in substantially the form attached hereto as Exhibit B.
  - 4. Warrants.** In partial consideration for its services in connection with the Business Combination, among other things, concurrently with the execution of this New Agreement, the Company shall issue to AFH Advisory five-year warrants to purchase 1,063,981 shares of common stock of the Company (the “Warrant Stock”), at an exercise price of \$1.00 per share (the “Exercise Price”), in substantially the form attached hereto as Exhibit C (the “Warrant”), pursuant to which, among other things: (a) AFH Advisory shall have normal and customary piggyback registration rights with respect to the Warrant Stock, as further set forth in Section 10 of the Warrant, (b) AFH Advisory may elect to exercise the Warrant, or any portion thereof, on a cashless basis, as further set forth in Section 1(b) of the Warrant, and (c) the Exercise Price shall be adjusted whenever the Company reduces the exercise price of any existing warrants (or any other security exercisable for, or convertible into, shares of common stock of the Company), or issues additional warrants (or any other security exercisable for, or convertible into, shares of common stock of the Company), as further set forth in Section 2(c) of the Warrant.
  - 5. Board Oversight.** For a period of two (2) years following the date hereof, AFH Advisory shall have a “board oversight right,” pursuant to which, among other things, it shall have the right to approve two members of the Company’s board of directors, such approval not to be unreasonably withheld.
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6. **Advisory Role.** For a period of two (2) years from the date hereof, AFH Advisory shall have the non-exclusive right to act as advisor to the Company on any proposed financings and/or mergers and acquisitions, to be separately engaged on a deal by deal basis.
  7. **Confidentiality.** Each party agrees to keep confidential all information obtained by it from the other party concerning the other party or any of its business transactions, to return to the other party any documents or copies thereof received or obtained by it from the other party. Further, except as and to the extent required by law, without the prior written consent of the other party, neither party shall make any public statement, common or communication with respect to, or otherwise disclose or permit the disclosure of, any discussions between the parties and/or relating to either party. If a party is required by law to make any such disclosure, such party must first provide to the other party the content of the proposed disclosure, the reasons that such disclosure is required by law, and the time and place the disclosure will be made.
  8. **Termination.** This New Agreement may be terminated by: (i) the mutual written consent of the Company and AFH Advisory; or (ii) upon written election of either party upon a material breach of any terms or conditions of this New Agreement and failure to cure such breach within thirty (30) days of receipt of written notice by the terminating party.
  9. **Binding Provisions.** The provisions set forth in this New Agreement are intended to and do constitute the binding and legal agreement between the parties, enforceable against the parties in accordance with its terms. Except as otherwise set forth herein, the parties have no further rights or obligations with respect to the Sections in the Letter of Intent entitled “Offering”, “Sale of Affiliate Shares”, “Company Financial Representation”, “Make Good Provision”, “Right to Future Financings”, “Right to Approve Management”, “Right to Appoint Directors; Right to Approve Independent Directors”, “Right to Approve Professionals”, “Lock-Up Agreement”, and “Investor Relations Firm”, and references to such Sections elsewhere in the Letter of Intent. In the event of any inconsistency between this New Agreement and the Letter of Intent, the terms of this New Agreement shall control.
  10. **Governing Law, Dispute Resolution and Jurisdiction.** This New Agreement shall be governed by and construed in accordance with the laws of California. Any controversy arising out of or concerning this New Agreement shall be determined by arbitration upon the initiation of either party, and shall be settled and conclusively resolved by and under the rules of the American Arbitration Association. The cost of such arbitrator shall initially be borne equally by the parties provided, however, that the prevailing party in any such arbitration shall be entitled to recover, in addition to any other appropriate amounts, its reasonable costs and expenses associated with such arbitration, including the cost of such arbitrator and reasonable attorney’s fees. The arbitration shall be conducted in Los Angeles, California and the written decision of the arbitrator shall be final and binding on the parties and enforceable in any court of competent jurisdiction. This New Agreement shall be governed by and construed in accordance with the laws of the State of California without giving effect to the conflicts of laws principles thereof. All disputes, controversies or claims arising out of or relating to this New Agreement shall be brought in Federal Court in California or in the Superior Court located in Los Angeles, California. The parties hereby irrevocably waive any objection to jurisdiction and venue or any action instituted hereunder and shall not assert any defense based on lack of jurisdiction or venue or based upon *forum non conveniens*. The parties agree to submit to the *in personam* jurisdiction of such courts and hereby irrevocably waive trial by jury. The prevailing party in any such dispute shall be entitled to recover from the other party its reasonable attorneys’ fees, costs and expenses.
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**11. Counterparts.** This New Agreement may be signed in two or more counterparts, each of which shall constitute an original, and all of which together shall constitute one and the same agreement. The exchange of copies of this New Agreement and of signature pages by facsimile transmission or by email transmission in portable digital format, or similar format, shall constitute effective execution and delivery of such instrument(s) as to the parties and may be used in lieu of the original for all purposes. Signatures of the parties transmitted by facsimile or by email transmission in portable digital format, or similar format, shall be deemed to be their original signatures.

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Please acknowledge your acceptance of your agreement to the foregoing by signing and returning to the undersigned as soon as possible a counterpart of this Amendment.

Very truly yours,

TARGETED MEDICAL PHARMA, INC.

By: /s/ William E. Shell

Name: William E. Shell, MD

Title: Chief Executive Officer

ACCEPTED AND AGREED TO AS OF JULY 25, 2012:

AFH Holding and Advisory, LLC

By: /s/ Amir F. Heshmatpour

Name: Amir F. Heshmatpour

Title: Managing Director

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Targeted Medical Pharma, Inc.  
2980 Beverly Glen Circle  
Suite 301  
Los Angeles, California 9077

July 25, 2012

AFH Holding and Advisory, LLC  
9595 Wilshire Boulevard  
Suite 700  
Beverly Hills, California 90212

Gentlemen:

Reference is hereby made to the letter agreement (the "Letter Agreement"), dated as of the date hereof, by and between Targeted Medical Pharma, Inc. (the "Company") and AFH Holding and Advisory, LLC ("AFH Advisory"). The parties desire to clarify the Letter Agreement and clarify their understanding of certain provisions of the Letter Agreement as follows:

1. The parties acknowledge that their understanding of Paragraph 5 ("*Board Oversight*") is as follows:

For a period of two (2) years from the date of the Letter Agreement, AFH has the right to disapprove of two nominees for director chosen by the board of directors of the Company.

2. The parties acknowledge that their understanding of Paragraph 6 ("*Advisory Role*") is as follows:

With respect to any specific financing or merger/acquisition the Company engages in during this two-year period, the Company may choose not to retain AFH as an advisor.

Please acknowledge your acceptance of your agreement to the foregoing by signing and returning to the undersigned as soon as possible a counterpart of this letter agreement.

Very truly yours,

TARGETED MEDICAL PHARMA, INC.

By: /s/ William E. Shell  
Name: William E. Shell, MD  
Title: Chief Executive Officer

ACCEPTED AND AGREED TO AS OF JULY 25, 2012:

AFH Holding and Advisory, LLC

By: /s/ Amir F. Heshmatpour  
Name: Amir F. Heshmatpour  
Title: Managing Director

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**AMENDMENT NO. 2 TO AGREEMENT AND PLAN OF REORGANIZATION**

AMENDMENT NO. 2 TO THE AGREEMENT AND PLAN OF REORGANIZATION (this "Amendment") made effective as of August 13, 2012 by and between AFH Holding and Advisory, LLC ("AFH"), Targeted Medical Pharma, Inc. ("Targeted"), William E. Shell, MD ("Shell"), the Estate of Elizabeth Charavustra (the "Estate") and Kim Giffoni ("Giffoni").

**WITNESSETH:**

WHEREAS, AFH Acquisition III, Inc. ("AFH III"), AFH, Targeted, TMP Merger Sub, Inc. ("TMP Sub"), AFH Merger Sub, Inc. ("AFH Merger Sub"), Shell, Elizabeth Charavustra and Giffoni entered into an Agreement and Plan of Reorganization, dated as of January 31, 2011, and amended as of October 17, 2011 (hereinafter the "Merger Agreement");

WHEREAS, pursuant to the Merger Agreement, AFH III, TMP Sub and AFH Merger Sub ceased to exist upon the consummation of the Merger.

NOW, THEREFORE, the parties hereto agree to amend the Merger Agreement as follows, effective as of the date hereof:

1. All capitalized terms used and not defined herein shall have the meanings ascribed thereto in the Merger Agreement.
2. Section 3.01 shall be deleted in its entirety.

The parties hereby agree that except as specifically provided in and modified by this Amendment, the Merger Agreement is in all other respects hereby ratified and confirmed and references to the Merger Agreement shall be deemed to refer to the Merger Agreement as modified by this Amendment.

\* \* \* \* \*

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IN WITNESS WHEREOF, the undersigned have executed this Amendment as of the day and year first written above.

**AFH HOLDING AND ADVISORY, LLC**

By: /s/ Amir F. Heshmatpour  
Name: Amir F. Heshmatpour  
Title: Managing Partner

**TARGETED MEDICAL PHARMA, INC.**

By: /s/ William E. Shell  
Name: William E. Shell, MD  
Title: Chief Executive Officer

/s/ William E. Shell  
**William E. Shell, MD**

**The Estate of Elizabeth Charuvastra**

By: /s/ William E. Shell  
**Name:** William E. Shell, MD  
**Title:** Executor

/s/ Kim Giffoni  
**Kim Giffoni**

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**NEITHER THESE SECURITIES NOR THE SECURITIES INTO WHICH THESE SECURITIES ARE CONVERTIBLE HAVE BEEN REGISTERED WITH THE SECURITIES AND EXCHANGE COMMISSION IN RELIANCE UPON AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "1933 ACT"), AND, ACCORDINGLY, MAY NOT BE OFFERED OR SOLD EXCEPT PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT OR PURSUANT TO AN AVAILABLE EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE 1933 ACT.**

**SECURED CONVERTIBLE PROMISSORY NOTE**

Los Angeles, California

\$585,448

**Issue Date: July 20, 2012**

**FOR VALUE RECEIVED**, TARGETED MEDICAL PHARMA, INC., a Delaware corporation (hereinafter called the "Borrower"), hereby promises to pay to the order of AFH HOLDING AND ADVISORY, LLC, a Delaware limited liability company, or its registered assigns (the "Holder"), the sum of FIVE HUNDRED EIGHTY FIVE THOUSAND FOUR HUNDRED FORTY EIGHT AND 00/100 DOLLARS (\$585,448) (the "Principal Amount"), on July \_\_, 2014 (the "Maturity Date"). The unpaid Principal Amount from time to time outstanding on this Secured Convertible Promissory Note (the "Note") shall bear interest at the rate of EIGHT AND ONE HALF PERCENT (8.5%) per annum ("Interest"), until the same becomes due and payable, whether at maturity or upon acceleration or by prepayment or otherwise. Interest shall be payable quarterly in arrears on the unpaid Principal Amount of the Note on each March 31st, June 30th, September 30th and December 31st after the issue date of the Note, up until the same becomes due and payable, whether at maturity or upon acceleration or by prepayment or otherwise (each such payment, an "Interest Payment"). Each Interest Payment shall be made, at the Holder's option, in either cash or shares of common stock of the Borrower, no par value per share ("Common Stock"). If the Interest Payment is made in shares of Common Stock, the number of shares to be received by the Holder shall be determined as set forth in Section 2(c) hereof. At the Holder's option, any Interest not paid within ten (10) days after the date due hereunder may be added to the Principal Amount of this Note and, if added to the Principal Amount, shall bear interest from its due date at the applicable interest rate specified herein. Any amount of principal or Interest on this Note which is not paid when due shall bear interest at the rate of FIFTEEN PERCENT (15%) per annum from the due date thereof until the same is paid ("Default Interest"). Interest and Default Interest shall be computed on the basis of a 365-day year and the actual number of days elapsed and shall be payable at the Maturity Date. Except as otherwise set forth herein, all payments due hereunder shall be made in lawful money of the United States of America. All payments shall be made at such address as the Holder shall hereafter give to the Borrower by written notice made in accordance with the provisions of this Note. Whenever any amount expressed to be due by the terms of this Note is due on any day which is not a Business Day, the same shall instead be due on the next succeeding day which is a Business Day. As used in this Note, the term "Business Day" shall mean any day other than a Saturday, Sunday or a day on which commercial banks in the city of New York, New York are authorized or required by law or executive order to remain closed. Notwithstanding any provision contained herein, the total liability of Borrower for payment pursuant hereto, including, without limitation late charges, shall not exceed the maximum amount of interest permitted by law to be charged, collected, or received from the Borrower, and if any payments by Borrower include interest in excess of such a maximum amount, the Holder shall apply such excess to the reduction of the unpaid Principal Amount due pursuant hereto, or if none is due, such excess shall be refunded to the Borrower. This Note is being issued by the Borrower to the Holder, pursuant to a letter agreement (the "Agreement") by and between the Borrower and the Holder, dated as of even date herewith. Each capitalized term used herein, and not otherwise defined, shall have the meaning ascribed thereto in the Agreement.

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The following terms shall apply to this Note:

**ARTICLE I.  
PREPAYMENT**

**1.1 Borrower's Prepayment Option.** Notwithstanding anything to the contrary contained herein, at Borrower's option at any time, upon fifteen (15) days prior written notice, the Borrower shall have the right to prepay the entire amount due to the Holder pursuant to the Note (the "Prepayment Option"). On the 16th day following such notice, the Borrower shall make payment to the Holder of an amount in cash equal to the sum of (a) the Principal Amount of the Note outstanding on such day plus (b) accrued and unpaid Interest on such unpaid Principal Amount plus (c) Default Interest, if any, on the amounts referred to in clauses (a) and (b) (the "Prepayment Amount"). If the Borrower fails to make such payment within one (1) Business Day of such date the Borrower shall be subject to a penalty of .005 multiplied by the Prepayment Amount for every additional Business Day on which such payment is not made.

**1.2 Holder's Prepayment Option.** Notwithstanding anything to the contrary contained herein, at Holder's option, Holder shall have the right at any time to be prepaid, in whole or in part, any amounts due under the terms of this Note from the proceeds of any offering or offerings of the Borrower's securities, as follows:

- (a) 12.5% of the proceeds from any offering or offerings resulting in net proceeds to the Borrower of an aggregate of less than \$1,000,000;
- (b) 25% of the proceeds from any offering or offerings resulting in net proceeds to the Borrower of an aggregate of between \$1,000,000 and \$1,999,999;
- (c) 50% of the proceeds from any offering or offerings resulting in net proceeds to the Borrower of an aggregate of between \$2,000,000 and \$2,999,999;

(d) full payment from any offering or offerings resulting in net proceeds to the Borrower of an aggregate of \$3,000,000 or more.

In order to exercise such right, Holder shall deliver a written notice of prepayment to the Borrower. The Borrower shall make payment to the Holder of an amount in cash equal to the sum indicated in such notice within three (3) Business Days following the date on which notice of prepayment is delivered.

**1.3 Reduction of Principal Amount for Certain Expenses.** The Borrower has advanced \$250,000 (the “Advance”) to the Holder, to be used for expenses, including the Holder’s advisory fees and expenses, in connection with a transaction relating to the purchase and sale of certain of the Borrower’s receivables (the “Receivables Transaction”). As soon as practicable following the issuance of this Note, the Holder shall deliver to the Borrower (a) a written notice setting forth in reasonable detail the amounts of all expenses actually incurred on behalf of the Borrower in connection with the Receivables Transaction (the “Expenses”), (b) copies of all invoices related to the Expenses, and (c) this signed original Note. The Principal Amount of the Note shall be reduced by an amount equal to the difference between the amount of the Advance and the aggregate amount of the Expenses, if any. Within five (5) Business Days following the Holder’s delivery of such written notice to the Borrower, the Borrower, at its expense, will cause to be issued in the name of, and delivered to, the Holder, or as such Holder may direct, a new Note of like tenor in the adjusted Principal Amount.

## ARTICLE II.

### CONVERSION

#### 2.1 Conversion.

(a) After the Issue Date, the Holder shall have the right (the “Conversion Right”), on the terms set forth in this Section 2.1, to convert the Principal Amount of this Note, and any Interest and/or Default Interest when due and payable, into shares of Common Stock of the Borrower, on the terms and conditions hereinafter set forth.

(b) In the event that the Holder elects to convert all or any portion of this Note into shares of Common Stock, the Holder shall give written notice of such election by delivering to the Borrower an executed and completed notice of conversion (the “Notice of Conversion”), such Notice of Conversion shall provide a breakdown in reasonable detail of the Principal Amount, accrued and unpaid Interest and/or Default Interest being converted. On each Conversion Date (as hereinafter defined) and in accordance with the Notice of Conversion, the Holder shall make the appropriate reduction to the Principal Amount and accrued and unpaid Interest and/or Default Interest as entered in its records and shall provide written notice thereof to the Borrower within two (2) Business Days after the Conversion Date. Each date on which a Notice of Conversion is delivered to the Borrower in accordance with the provisions hereof shall be deemed, for all purposes of this Note, to be the “Conversion Date”. Pursuant to the terms of the Notice of Conversion, the Borrower will issue instructions to the transfer agent (together with such other documents as the transfer agent may request) within two (2) Business Days of the date of the delivery to the Borrower of the Notice of Conversion. The Borrower shall use its best efforts to cause its transfer agent to transmit the certificates representing the Common Stock issuable upon full or partial conversion of this Note to any address or depository directed by the Holder within five (5) Business Days after receipt by the Borrower of the Notice of Conversion.

(c) The number of shares of Common Stock to be issued upon any conversion of this Note (the “Conversion Shares”) shall be determined by dividing that portion of the Principal Amount and any Interest and/or Default Interest to be converted, if any, by a price equal to the lesser of (i) \$1.00, or (ii) the average of the lowest three (3) Trading Prices (as defined below) for the Common Stock during the ten (10) Trading Day period ending on the latest complete Trading Day prior to the Conversion Date (the “Conversion Price”). “Trading Price” means, for any security as of any date, the closing bid price on the Over-the-Counter Bulletin Board, or applicable trading market (the “OTCBB”) as reported by a reliable reporting service (“Reporting Service”) designated by the Holder (i.e. Bloomberg) or, if the OTCBB is not the principal trading market for such security, the closing bid price of such security on the principal securities exchange or trading market where such security is listed or traded or, if no closing bid price of such security is available in any of the foregoing manners, the average of the closing bid prices of any market makers for such security that are listed in the “pink sheets” by the National Quotation Bureau, Inc. If the Trading Price cannot be calculated for such security on such date in the manner provided above, the Trading Price shall be the fair market value as mutually determined by the Borrower and the Holders. “Trading Day” shall mean any day on which the Common Stock is tradable for any period on the OTCBB, or on the principal securities exchange or other securities market on which the Common Stock is then being traded.

(d) The Conversion Price and number and kind of shares or other securities to be issued upon conversion is subject to adjustment from time to time upon the occurrence of certain events, as follows:

(i) Reclassification, etc. If the Borrower at any time shall, by reclassification or otherwise, change the Common Stock into the same or a different number of securities of any class or classes, the Principal Amount of this Note, and any accrued and unpaid Interest and/or Default Interest thereon, and fees incurred hereunder, shall thereafter be deemed to evidence the right to purchase an adjusted number of such securities and kind of securities as would have been issuable as the result of such change with respect to the Common Stock immediately prior to such reclassification or other change.

(ii) Stock Splits, Combinations and Dividends. If the shares of Common Stock outstanding at any time after the date hereof are subdivided or combined into a greater or smaller number of shares of Common Stock, or if a dividend is paid on the Common Stock in shares of Common Stock, the Conversion Price or the Conversion Shares to be issued, as the case may be, shall be proportionately reduced in case of subdivision of shares or stock dividend or proportionately increased in the case of combination of shares, in each such case by the ratio which the total number of shares of Common Stock outstanding immediately after such event bears to the total number of shares of Common Stock outstanding immediately prior to such event.

(e) Notwithstanding anything in this Note to the contrary, the Holder shall not convert this Note into that number of shares of Common Stock which would be in excess of the sum of (i) the number of shares of Common Stock beneficially owned by the Holder and its affiliates (other than shares of Common Stock which may be deemed beneficially owned through the ownership of the unexercised or unconverted portion of any other securities of the Borrower (subject to a limitation on conversion or exercise analogous to the limitation contained herein)) and (ii) the number of shares of Common Stock issuable upon the conversion of this Note held by the Holder and its affiliates with respect to which the determination of this proviso is being made which would result in beneficial ownership by the Holder and its affiliates of more than 9.9% of the outstanding shares of the Borrower's Common Stock. For purposes of the immediately preceding sentence, beneficial ownership shall be determined in accordance with Section 13(d) of the Securities Exchange Act of 1934, as amended, and Regulation 13D-G thereunder, except as otherwise provided in clause (i) of the preceding sentence. The Holder may waive the limitations set forth in this Section at its sole and absolute discretion by written notice of not less than sixty-one (61) days to the Borrower.

(f) The Borrower shall at all times reserve and keep available out of its authorized but unissued shares of Common Stock, solely for the purpose of providing for the conversion of the Note, such number of shares of Common Stock as shall from time to time equal the number of Conversion Shares issuable from time to time.

### ARTICLE III.

#### SECURITY

3.1 All of the obligations of the Borrower under the Note are secured by a security interest in and to the Borrower's rights to certain assets of the Borrower comprised of Allen Salick MD, Inc. open claims from October 8, 2007 through and including March 9, 2010, in the approximate value of \$2,658,000 (hereinafter, the "Collateral"), pursuant to the Security Agreement (the "Security Agreement") by and between the Borrower and the Holder, dated as of even date herewith. The Borrower hereby irrevocably authorizes the Holder at any time and from time to time to file in any Uniform Commercial Code jurisdiction any initial financing statements and amendments thereto that (i) indicate the Collateral regardless of whether any particular asset comprised in the Collateral falls within the scope of Article 9 of the Uniform Commercial Code of the State of California as amended from time to time ("CAUCC"), or any other Uniform Commercial Code jurisdiction; and (ii) contain any other information required by part 5 of Article 9 of the CAUCC for the sufficiency or filing office acceptance of any financing statement or amendment, including whether the Borrower is an organization, the type of organization and any organization identification number issued to the Borrower. The Borrower agrees to furnish any such information to the Holder promptly upon request. The Borrower also ratifies its authorization for the Holder to have filed in any Uniform Commercial Code jurisdiction any like initial financing statements or amendments thereto if filed prior to the date hereof with respect to the Collateral.

## ARTICLE IV

### CERTAIN COVENANTS

**4.1 Distributions on Capital Stock.** So long as the Borrower shall have any obligation under this Note, the Borrower shall not without the Holder's written consent (a) pay, declare or set apart for such payment, any dividend or other distribution (whether in cash, property or other securities) on shares of capital stock other than dividends on shares of Common Stock solely in the form of additional shares of Common Stock or (b) directly or indirectly or through any subsidiary make any other payment or distribution in respect of its capital stock except for distributions pursuant to any shareholders' rights plan which is approved by a majority of the Borrower's disinterested directors.

**4.2 Restriction on Stock Repurchases.** So long as the Borrower shall have any obligation under this Note, the Borrower shall not without the Holder's written consent redeem, repurchase or otherwise acquire (whether for cash or in exchange for property or other securities or otherwise) in any one transaction or series of related transactions any shares of capital stock of the Borrower or any warrants, rights or options to purchase or acquire any such shares.

**4.3 Borrowings.** So long as the Borrower shall have any obligation under this Note, the Borrower shall not, without the Holder's written consent, create, incur, assume or suffer to exist any liability for borrowed money, except (a) borrowings in existence or committed on the date hereof and of which the Borrower has informed Holder in writing prior to the date hereof, (b) indebtedness to trade creditors or financial institutions incurred in the ordinary course of business (c) borrowings from financial institutions where the primary purpose of the proceeds is for the general corporate use of the Borrower, or (d) borrowings, the proceeds of which shall be used to repay this Note.

**4.4 Sale of Assets.** So long as the Borrower shall have any obligation under this Note, the Borrower shall not, without the Holder's written consent, sell, lease or otherwise dispose (collectively, a "Disposition") of any significant portion of its assets, other than to a wholly-owned subsidiary of the Borrower, outside the ordinary course of business unless the proceeds of such Disposition shall be used to repay this Note. Any consent to the disposition of any assets may be conditioned on a specified use of the proceeds of disposition.

**4.5 Advances and Loans.** So long as the Borrower shall have any obligation under this Note, the Borrower shall not, without the Holder's written consent, lend money, give credit or make advances to any person, firm, joint venture or corporation, including, without limitation, officers, directors, employees, subsidiaries and affiliates of the Borrower, except loans, credits or advances (a) in existence or committed on the date hereof and which the Borrower has informed Holder in writing prior to the date hereof or (b) made in the ordinary course of business.

**4.6 Contingent Liabilities.** So long as the Borrower shall have any obligation under this Note, the Borrower shall not, without the Holder's written consent, assume, guarantee, endorse, contingently agree to purchase or otherwise become liable upon the obligation of any person firm, partnership, joint venture or corporation, except by the endorsement of negotiable instruments for deposit or collection and except assumptions, guarantees, endorsements and contingencies (a) in existence or committed on the date hereof and which the Borrower has informed Holder in writing prior to the date hereof, and (b) similar transactions in the ordinary course of business.

**ARTICLE V.**

**EVENTS OF DEFAULT**

**5.1 Events of Default.** Each of the following events shall be deemed an “Event of Default” under this Note:

(a) **Failure to Pay Principal or Interest.** The Borrower fails to pay the Principal Amount hereof or Interest thereon when due on this Note, whether at maturity, upon acceleration, or otherwise.

(b) **Breach of Covenants.** The Borrower breaches any material covenant or other material term or condition contained herein, or in the Agreement, and such breach continues for a period of thirty (30) days after written notice thereof to the Borrower from the Holder.

(c) **Breach of Representations and Warranties.** Any representation or warranty of the Borrower made herein or in any agreement, statement or certificate given in writing pursuant hereto or in connection herewith (including, without limitation, the Agreement), shall be false or misleading in any material respect when made and the breach of which has (or with the passage of time will have) a material adverse effect on the rights of the Holder with respect to this Note or the Agreement.

(d) **Receiver or Trustee.** The Borrower or any subsidiary of the Borrower shall make an assignment for the benefit of creditors, or apply for or consent to the appointment of a receiver or trustee for it or for a substantial part of its property or business, or such a receiver or trustee shall otherwise be appointed;

(e) **Judgments.** Any money judgment, writ or similar process shall be entered or filed against the Borrower or any subsidiary of the Borrower or any of its property or other assets for more than \$250,000, and shall remain un-vacated, un-bonded or un-stayed for a period of twenty (20) days unless otherwise consented to by the Holder, which consent will not be unreasonably withheld; or

(f) **Bankruptcy.** Bankruptcy, insolvency, reorganization or liquidation proceedings or other proceedings for relief under any bankruptcy law or any law for the relief of debtors shall be instituted by or against the Borrower or any subsidiary of the Borrower and if instituted against Borrower is not dismissed within sixty (60) days.



**5.2 Effect of Event of Default.** Upon the happening of any Event of Default, as set forth in Section 5.1 above, then, or at any time thereafter, and in each and every such case, unless such Event of Default shall have been waived in writing by the Holder (which waiver shall not serve as a waiver of any subsequent default) at the option of the Holder and in the Holder's sole discretion, the Holder may consider this Note immediately due and payable, without presentment, demand, protest or notice of any kind, all of which are hereby expressly waived, anything herein notwithstanding, and the Holder may immediately enforce any and all of the Holder's rights and remedies provided herein or any other right or remedy afforded by law.

## ARTICLE VI.

### PIGGYBACK REGISTRATION RIGHTS

#### 6.1 General.

(a) The Holder is hereby granted the right to "piggyback" the Conversion Shares issuable and/or issued upon the Principal Amount of this Note and the accrued and unpaid Interest and/or Default Interest thereon (such shares being referred to herein as "Registrable Securities") on each registration statement filed by the Borrower so long as the registration form to be used is suitable for the registration of the Registrable Securities (a "Piggyback Registration") (it being understood that the Form S-8 and Form S-4 may not be used for such purposes), all at the Borrower's cost and expense (except commissions or discounts and fees of any of the holders' own professionals, if any; it being understood that the Borrower shall not be obligated to pay the fees of more than one counsel for the holders of the Registrable Securities); provided, however, that this paragraph (a) shall not apply to any Registrable Securities if such Registrable Securities may then be sold within a six (6) month period under Rule 144 (assuming the holder's compliance with the provisions of the Rule) and the Borrower delivers an opinion to that effect to the transfer agent; and provided, further, that if the offering with respect to which a registration statement is filed is an underwritten primary or secondary offering of the Borrower's securities and the managing underwriter advises the Borrower in writing that in its opinion the number of securities requested to be included in such registration exceeds the number that can be sold in such offering without adversely affecting such underwriter's ability to effect an orderly distribution of such securities or otherwise adversely effecting such offering (including, without limitation, causing a diminution in the offering price of the Borrower's securities) the Borrower will include in such registration statement: (i) first, the securities being sold for the account of the Borrower; and (ii) second, the number of securities with respect to which the Borrower has granted rights to participate in such registration (including the Registrable Securities) that, in the opinion of such underwriter, can be sold pro rata among the respective holders of such securities on the basis of the amount of such securities then owned by each such holder. The Borrower shall give each holder of Registrable Securities at least fifteen (15) days written notice of the intended filing date of any registration statement, other than a registration statement filed on Form S-4 or Form S-8 and each holder of Registrable Securities shall have seven (7) days after receipt of such notice to notify the Borrower of its intent to include the Registrable Securities in the registration statement.

(b) If, at any time after giving written notice of its intention to register any securities and prior to the effective date of the registration statement filed in connection with such registration, the Borrower shall determine for any reason not to register or to delay registration of such securities, the Borrower may, at its election, give written notice of such determination to all holders of the Registrable Securities and (i) in the case of a determination not to register, shall be relieved of its obligation to register any Registrable Securities in connection with such abandoned registration and (ii) in the case of a determination to delay such registration of its securities, shall be permitted to delay the registration of such Registrable Securities for the same period as the delay in registering such other Borrower securities.

**6.2 Expenses.** The Borrower shall bear all fees and expenses attendant to registering the Registrable Securities (except any underwriters' discounts and commissions and fees of any of the holders' own professionals, if any; it being understood that the Borrower shall not be obligated to pay the fees of more than one counsel for the holders of the Registrable Securities). The Borrower agrees to use its best efforts to cause the filing required herein to become effective promptly and to qualify to register the Registrable Securities in such States as are reasonably requested by the holder(s); provided, however, that in no event shall the Borrower be required to register the Registrable Securities in a State in which such registration would cause (a) the Borrower to be obligated to register or license to do business in such State, or (b) the principal stockholders of the Borrower to be obligated to escrow any of their shares of capital stock of the Borrower.

**6.3 Indemnification.** The Borrower shall indemnify and hold harmless each holder of the Registrable Securities to be sold pursuant to any Registration Statement hereunder and each of such holder's officers, directors, employees, agents, partners, legal counsel and accountants, and each person, if any, who controls each of the foregoing within the meaning of Section 15 of the Securities Act or Section 20(a) of the 1934 Act, as amended, against all loss, claim, damage, expense or liability (including all reasonable attorneys' fees and other expenses reasonably incurred in investigating, preparing or defending against any claim whatsoever incurred by the indemnified party in any action or proceeding between the indemnitor and indemnified party or between the indemnified party and any third party or otherwise) to which any of them may become subject under the Securities Act, the Exchange Act or any other statute or at common law or otherwise under laws of foreign countries, arising from such registration statement or based upon any untrue statement or alleged untrue statement of a material fact contained in (a) any preliminary prospectus, registration statement or prospectus (as from time to time each may be amended and supplemented); (b) in any post-effective amendment or amendments or any new registration statement and prospectus in which is included the Registrable Securities; or (c) any application or other document or written communication (collectively called "application") executed by the Borrower or based upon written information furnished by the Borrower in any jurisdiction in order to qualify the Registrable Securities under the securities laws thereof or filed with the commission, any state securities commission or agency or any securities exchange; or the omission or alleged omission therefrom of a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading; unless such statement or omission is made in reliance upon, and in strict conformity with, written information furnished to the Borrower with respect to the holders expressly for use in a preliminary prospectus, registration statement or prospectus, or any amendment or supplement thereof, or in any application, as the case may be. The Borrower agrees promptly to notify the holders of the Registrable Securities of the commencement of any litigation proceedings against the Borrower or any of its officers, directors or controlling persons in connection with the issue and sale or resale of the Registrable Securities or in connection with any such registration statement or prospectus.

**ARTICLE VII**  
**MISCELLANEOUS**

**7.1 Failure or Indulgence Not Waiver.** No failure or delay on the part of the Holder in the exercise of any power, right or privilege hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any such power, right or privilege preclude other or further exercise thereof or of any other right, power or privileges. All rights and remedies existing hereunder are cumulative to, and not exclusive of, any rights or remedies otherwise available.

**7.2 Notices.** Unless otherwise provided, any notice required or permitted under this Note shall be given in writing and shall be deemed effectively given as hereinafter described (i) if given by personal delivery, then such notice shall be deemed given upon such delivery, (ii) if given by telex or facsimile, then such notice shall be deemed given upon receipt of confirmation of complete transmittal, (iii) if given by mail, then such notice shall be deemed given upon the earlier of (A) receipt of such notice by the recipient or (B) three days after such notice is deposited in first class mail, postage prepaid, and (iv) if given by an internationally recognized overnight air courier, then such notice shall be deemed given one business day after delivery to such carrier. All notices shall be addressed as follows:

If to the Borrower, to:

Targeted Medical Pharma, Inc.  
2980 Beverly Glen Circle, Suite 301  
Los Angeles, CA 90077  
Attn: \_\_\_\_\_  
Fax: \_\_\_\_\_

with a copy to:

If to the Holder, to:

AFH Holding and Advisory, LLC  
9595 Wilshire Boulevard, Suite 700  
Beverly Hills, CA 90212  
Attn: \_\_\_\_\_  
Fax: \_\_\_\_\_

with a copy to:

or, in each case, to such other address as the parties may hereinafter designate by like notice.

**7.3 Amendments.** This Note and any provision hereof may only be amended by an instrument in writing signed by the Borrower and the Holder. The term “Note” and all reference thereto, as used throughout this instrument, shall mean this instrument as originally executed, or if later amended or supplemented, then as so amended or supplemented.

**7.4 Assignability.** This Note shall be binding upon the Borrower and its successors and assigns, and shall inure to the benefit of the Holder and its successors and assigns. Each transferee of this Note must be an “accredited investor” (as defined in Rule 501(a) of the 1933 Act). Notwithstanding anything in this Note to the contrary, this Note may be pledged as collateral in connection with a bona fide margin account or other lending arrangement.

**7.5 Governing Law.** THIS NOTE SHALL BE ENFORCED, GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF CALIFORNIA APPLICABLE TO AGREEMENTS MADE AND TO BE PERFORMED ENTIRELY WITHIN SUCH STATE, WITHOUT REGARD TO THE PRINCIPLES OF CONFLICT OF LAWS. THE BORROWER HEREBY SUBMITS TO THE EXCLUSIVE JURISDICTION OF THE UNITED STATES FEDERAL COURTS LOCATED IN LOS ANGELES, CALIFORNIA WITH RESPECT TO ANY DISPUTE ARISING UNDER THIS NOTE, THE AGREEMENTS ENTERED INTO IN CONNECTION HERewith OR THE TRANSACTIONS CONTEMPLATED HEREBY OR THEREBY. BOTH PARTIES IRREVOCABLY WAIVE THE DEFENSE OF AN INCONVENIENT FORUM TO THE MAINTENANCE OF SUCH SUIT OR PROCEEDING. BOTH PARTIES FURTHER AGREE THAT SERVICE OF PROCESS UPON A PARTY MAILED BY FIRST CLASS MAIL SHALL BE DEEMED IN EVERY RESPECT EFFECTIVE SERVICE OF PROCESS UPON THE PARTY IN ANY SUCH SUIT OR PROCEEDING. NOTHING HEREIN SHALL AFFECT EITHER PARTY’S RIGHT TO SERVE PROCESS IN ANY OTHER MANNER PERMITTED BY LAW. BOTH PARTIES AGREE THAT A FINAL NON-APPEALABLE JUDGMENT IN ANY SUCH SUIT OR PROCEEDING SHALL BE CONCLUSIVE AND MAY BE ENFORCED IN OTHER JURISDICTIONS BY SUIT ON SUCH JUDGMENT OR IN ANY OTHER LAWFUL MANNER. THE PARTY WHICH DOES NOT PREVAIL IN ANY DISPUTE ARISING UNDER THIS NOTE SHALL BE RESPONSIBLE FOR ALL FEES AND EXPENSES, INCLUDING REASONABLE ATTORNEYS’ FEES, INCURRED BY THE PREVAILING PARTY IN CONNECTION WITH SUCH DISPUTE.

**7.6 Denominations.** At the request of the Holder, upon surrender of this Note, the Borrower shall promptly issue new Notes in the aggregate outstanding Principal Amount hereof, in the form hereof, in such denominations as the Holder shall request.

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**IN WITNESS WHEREOF**, Borrower has caused this Note to be signed in its name by its duly authorized representative this 20th day of July, 2012.

**TARGETED MEDICAL PHARMA, INC.**

By: /s/ William E. Shell

Name: William E. Shell, M.D.

Title: Chief Executive Officer

**SECURITY AGREEMENT**

**THIS SECURITY AGREEMENT** (this “Security Agreement”), is made as of July 20, 2012, by and between Targeted Medical Pharma, Inc., a Delaware corporation, having an address at 2980 Beverly Glen Circle, Suite 301, Los Angeles, CA 90077 (the “Obligor” or “Company”), and AFH Holding and Advisory, LLC, a Delaware limited liability company, having an address at 9595 Wilshire Boulevard, Suite 700, Beverly Hills, CA 90212 (the “Secured Party”). (The Company and the Secured Party may hereinafter be referred to singularly as a “party,” and collectively as the “parties”).

**WITNESSETH**

**WHEREAS**, concurrently herewith, the Obligor is entering into a letter agreement with the Secured Party (the “Letter Agreement”), pursuant to which, in consideration for past services rendered, the Obligor will issue to the Secured Party (a) a Secured Convertible Promissory Note in the principal amount of \$585,448 (the “Note”); and (b) warrants to purchase 1,063,981 shares of the Company’s common stock (the “Warrants”); and

**WHEREAS**, the Obligor has agreed to execute and deliver to the Secured Party this Security Agreement for the benefit of the Secured Party and to grant to the Secured Party a security interest in certain of the Obligor’s assets, as set forth in Section 1(a) below, to secure the prompt payment, performance and discharge in full of all of the Obligor’s obligations under the Security Agreement, the Note and the Warrants.

**NOW, THEREFORE**, in consideration of the agreements herein contained and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties hereto hereby agree as follows:

1. **Certain Definitions.** As used in this Security Agreement, the following terms shall have the meanings set forth in this Section 1. Terms used but not otherwise defined in this Security Agreement that are defined in Article 9 of the UCC shall have the respective meanings given such terms in Article 9 of the UCC. Each capitalized term used herein, and not otherwise defined, shall have the meaning ascribed thereto in the Letter Agreement.

(a) “Collateral” means the collateral in which the Secured Party is granted a security interest by this Security and which shall include the following, whether presently owned or existing or hereafter acquired or coming into existence, and all additions and accessions thereto and all substitutions and replacements thereof, and all proceeds, products and accounts thereof, including, without limitation, all proceeds from the sale or transfer of the Collateral and of insurance covering the same and of any tort claims in connection therewith:

(i) All of the Obligor’s rights in and to Allen Salick MD, Inc. open claims from October 8, 2007 through and including March 9, 2010, in the approximate value of \$2,658,000, as further set forth on **Schedule A** hereto; and

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(ii) All of the Obligor's documents, instruments and chattel paper, files, records, books of account, business papers, computer programs and the products and proceeds of all of the foregoing Collateral set forth in clause (i) above, if any.

(b) "Obligations" means all of the Obligor's obligations under this Security Agreement, the Letter Agreement, the Note and the Warrants, in each case, whether now or hereafter existing, voluntary or involuntary, direct or indirect, absolute or contingent, liquidated or unliquidated, whether or not jointly owed with others, and whether or not from time to time decreased or extinguished and later decreased, created or incurred, and all or any portion of such obligations or liabilities that are paid, to the extent all or any part of such payment is avoided or recovered directly or indirectly from the Secured Party as a preference, fraudulent transfer or otherwise as such obligations may be amended, supplemented, converted, extended or modified from time to time.

(c) "UCC" means the Uniform Commercial Code, as currently in effect in the State of California.

2. **Grant of Security Interest.** To secure the complete and timely payment, performance and discharge in full, as the case may be, of all of the Obligations, except for Permitted Liens (as hereinafter defined), the Obligor hereby, unconditionally and irrevocably, pledges, grants and hypothecates to the Secured Party, a continuing security interest in, a continuing lien upon, an unqualified right to possession and disposition of and a right of set-off against, in each case to the fullest extent permitted by law, all of the Obligor's right, title and interest of whatsoever kind and nature in and to the Collateral (the "Security Interest").

3. **Representations, Warranties, Covenants and Agreements of the Obligor.** The Obligor represents and warrants to, and covenants and agrees with, the Secured Party as follows:

(a) The Obligor has the requisite corporate power and authority to enter into this Security Agreement and otherwise to carry out its obligations hereunder. The execution, delivery and performance by the Obligor of this Security Agreement and the filings contemplated herein have been duly authorized by all necessary action on the part of the Obligor and no further action is required by the Obligor. This Security Agreement constitutes a legal, valid and binding obligation of the Obligor enforceable in accordance with its terms, except as enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium or similar laws affecting the enforcement of creditor's rights generally.

(b) The Obligor represents and warrants that it has no place of business or offices where its respective books of account and records are kept (other than temporarily at the offices of its attorneys or accountants), except as set forth on **Schedule B** attached hereto;

(c) Except as to those liens existing as of the date hereof that were disclosed to the Secured Party by the Obligor and are set forth on the attached **Schedule C** (the "Permitted Liens"), the Obligor is the sole owner of the Collateral (except for non-exclusive licenses granted by the Obligor in the ordinary course of business), free and clear of any liens, security interests, encumbrances, rights or claims, and is fully authorized to grant the Security Interest in and to pledge the Collateral. Except as to the Permitted Liens, there is not on file in any governmental or regulatory authority, agency or recording office an effective financing statement, security agreement, license or transfer or any notice of any of the foregoing (other than those that have been filed in favor of the Secured Party pursuant to this Security Agreement) covering or affecting any of the Collateral. Except as to the Permitted Liens, so long as this Security Agreement shall be in effect, the Obligor shall not execute and shall not knowingly permit to be on file in any such office or agency any such financing statement or other document or instrument (except to the extent filed or recorded in favor of the Secured Party pursuant to the terms of this Security Agreement).



(d) No part of the Collateral has been judged invalid or unenforceable. No written claim has been received that any Collateral or the Obligor's use of any Collateral violates the rights of any third party. There has been no adverse decision to the Obligor's claim of ownership rights in or exclusive rights to use the Collateral in any jurisdiction or to the Obligor's right to keep and maintain such Collateral in full force and effect, and there is no proceeding involving said rights pending or, to the best knowledge of the Obligor, threatened before any court, judicial body, administrative or regulatory agency, arbitrator or other governmental authority.

(e) The Obligor shall at all times maintain its books of account and records relating to the Collateral at its principal place of business and may not relocate such books of account and records unless it delivers to the Secured Party at least 30 days prior to such relocation (i) written notice of such relocation and the new location thereof (which must be within the United States) and (ii) evidence that appropriate financing statements and other necessary documents have been filed and recorded and other steps have been taken to perfect the Security Interest to create in favor of the Secured Party a valid, perfected and continuing lien in the Collateral.

(f) This Security Agreement creates in favor of the Secured Party a valid security interest in the Collateral securing the payment and performance of the Obligations and, upon making the filings described in the immediately following sentence, a perfected security interest in such Collateral. Except for the filing of financing statements on Form-1 under the UCC with the jurisdictions indicated on **Schedule D**, attached hereto, no authorization or approval of or filing with or notice to any governmental authority or regulatory body is required either (i) for the grant by the Obligor of, or the effectiveness of, the Security Interest granted hereby or for the execution, delivery and performance of this Security Agreement by the Obligor or (ii) for the perfection of or exercise by the Secured Party of its rights and remedies hereunder.

(g) The Obligor hereby irrevocably authorizes the Secured Party at any time and from time to time to file in any Uniform Commercial Code jurisdiction any initial financing statements and amendments thereto that (a) indicate the Collateral regardless of whether any particular asset comprised in the Collateral falls within the scope of Article 9 of the Uniform Commercial Code of the State of California as amended from time to time ("CAUCC"), or any other Uniform Commercial Code jurisdiction; and (b) contain any other information required by part 5 of Article 9 of the CAUCC for the sufficiency or filing office acceptance of any financing statement or amendment, including whether the Obligor is an organization, the type of organization and any organization identification number issued to the Obligor. The Obligor agrees to furnish any such information to the Secured Party promptly upon request. The Obligor also ratifies its authorization for the Secured Party to have filed in any Uniform Commercial Code jurisdiction any like initial financing statements or amendments thereto if filed prior to the date hereof with respect to the Collateral.

(h) The execution, delivery and performance of this Security Agreement does not conflict with or cause a breach or default, or an event that with or without the passage of time or notice, shall constitute a breach or default, under any agreement to which the Obligor is a party or by the Obligor is bound. No consent (including, without limitation, from stockholders or creditors of the Obligor) is required for the Obligor to enter into and perform its obligations hereunder.

(i) The Obligor shall at all times maintain the liens and Security Interest provided for hereunder as valid and perfected liens and security interests in the Collateral in favor of the Secured Party until this Security Agreement and the Security Interest hereunder shall be terminated pursuant to Section 11. The Obligor hereby agrees to defend the same against any and all persons. The Obligor shall safeguard and protect all Collateral for the account of the Secured Party. At the request of the Secured Party, the Obligor will pay the cost of filing one or more financing statements pursuant to the UCC (or any other applicable statute) in form reasonably satisfactory to the Secured Party in all public offices wherever filing is, or is deemed by the Secured Party to be, necessary or desirable to effect the rights and obligations provided for herein. Without limiting the generality of the foregoing, the Obligor shall pay all fees, taxes and other amounts necessary to maintain the Collateral and the Security Interest hereunder, and the Obligor shall obtain and furnish to the Secured Party from time to time, upon demand, such releases and/or subordinations of claims and liens which may be required to maintain the priority of the Security Interest hereunder.

(j) The Obligor will not transfer, pledge, hypothecate, encumber, license (except for non-exclusive licenses granted by the Obligor in the ordinary course of business), sell (except for sales of inventory in the ordinary course of business) or otherwise dispose of any of the Collateral without the prior written consent of the Secured Party.

(k) The Obligor shall keep and preserve its Equipment, Inventory and other tangible Collateral in good condition, repair and order and shall not operate or locate any such Collateral (or cause to be operated or located) in any area excluded from insurance coverage.

(l) The Obligor shall, within ten (10) days of obtaining knowledge thereof, advise the Secured Party promptly, in sufficient detail, of any substantial change in the Collateral, and of the occurrence of any event which would have a material adverse effect on the value of the Collateral or on the Secured Party's security interest therein.

(m) The Obligor shall promptly execute and deliver to the Secured Party such further deeds, mortgages, assignments, security agreements, financing statements or other instruments, documents, certificates and assurances and take such further action as the Secured Party may from time to time request and may in its sole discretion deem necessary to perfect, protect or enforce its security interest in the Collateral.

(n) The Obligor shall permit the Secured Party and their representatives and agents to inspect the Collateral at any time and to make copies of records pertaining to the Collateral as may be requested by the Secured Party from time to time.

(o) The Obligor will take all steps reasonably necessary to diligently pursue and seek to preserve, enforce and collect any rights, claims, causes of action and accounts receivable in respect of the Collateral.

(p) The Obligor shall promptly notify the Secured Party in sufficient detail upon becoming aware of any attachment, garnishment, execution or other legal process levied against any Collateral and of any other information received by the Obligor that may materially affect the value of the Collateral, the Security Interest or the rights and remedies of the Secured Party hereunder.

(q) All information heretofore, herein or hereafter supplied to the Secured Party by or on behalf of the Obligor with respect to the Collateral is accurate and complete in all material respects as of the date furnished.

4. **Defaults.** The following events shall be "Events of Default":

(a) A breach by the Obligor of its material obligations under the Letter Agreement, Note or Warrants, and failure to cure such breach for ten (10) days after receipt by the Obligor of notice of such breach from the Secured Party;

(b) Any representation or warranty of the Obligor in this Security Agreement shall prove to have been incorrect in any material respect when made; and

(c) The material failure by the Obligor to observe or perform any of its material obligations hereunder for ten (10) days after receipt by the Obligor of notice of such failure from the Secured Party.

5. **Duty To Hold In Trust.** Upon the occurrence of any Event of Default and at any time thereafter, the Obligor shall, upon receipt by it of any revenue, income or other sums subject to the Security Interest, whether payable pursuant to the Letter Agreement, the Note, or otherwise, or of any check, draft, debenture, trade acceptance or other instrument evidencing an obligation to pay any such sum, hold the same in trust for the Secured Party and shall forthwith endorse and transfer any such sums or instruments, or both, to the Secured Party for application to the satisfaction of the Obligations.

6. **Rights and Remedies Upon Default.** Upon occurrence of any Event of Default and at any time thereafter, the Secured Party shall have the right to exercise all of the remedies conferred hereunder and under the Letter Agreement, and the Secured Party shall have all the rights and remedies of a secured party under the UCC and/or any other applicable law (including the Uniform Commercial Code of any jurisdiction in which any Collateral is then located). The Secured Party shall have the following rights and powers:

(a) The Secured Party shall have the right to take possession of the Collateral and, for that purpose, enter, with the aid and assistance of any person, any premises where the Collateral, or any part thereof, is or may be placed and remove the same, and the Obligor shall assemble the Collateral and make it available to the Secured Party at places which the Secured Party shall reasonably select, whether at the Obligor's premises or elsewhere, and make available to the Secured Party, without rent, all of the Obligor's respective premises and facilities for the purpose of the Secured Party taking possession of, removing or putting the Collateral in saleable or disposable form.

(b) The Secured Party shall have the right to operate the business of the Obligor using the Collateral and shall have the right to assign, sell, lease or otherwise dispose of and deliver all or any part of the Collateral, at public or private sale or otherwise, either with or without special conditions or stipulations, for cash or on credit or for future delivery, in such parcel or parcels and at such time or times and at such place or places, and upon such terms and conditions as the Secured Party may deem commercially reasonable, all without (except as shall be required by applicable statute and cannot be waived) advertisement or demand upon or notice to the Obligor or right of redemption of the Obligor, which are hereby expressly waived. Upon each such sale, lease, assignment or other transfer of Collateral, the Secured Party may, unless prohibited by applicable law which cannot be waived, purchase all or any part of the Collateral being sold, free from and discharged of all trusts, claims, right of redemption and equities of the Obligor, which are hereby waived and released.

#### **7. Applications of Proceeds.**

(a) The proceeds of any such sale, lease or other disposition of the Collateral hereunder shall be applied first, to the expenses of retaking, holding, storing, processing and preparing for sale, selling, and the like (including, without limitation, any taxes, fees and other costs incurred in connection therewith) of the Collateral, to the reasonable attorneys' fees and expenses incurred by the Secured Party in enforcing its rights hereunder and in connection with collecting, storing and disposing of the Collateral, and then to satisfaction of the Obligations, and to the payment of any other amounts required by applicable law, after which the Secured Party shall pay to the Obligor any surplus proceeds. If, upon the sale, license or other disposition of the Collateral, the proceeds thereof are insufficient to pay all amounts to which the Secured Party is legally entitled, the Obligor will be liable for the deficiency, together with interest thereon, at the rate of 15% per annum (the "Default Rate"), and the reasonable fees of any attorneys employed by the Secured Party to collect such deficiency. To the extent permitted by applicable law, the Obligor waives all claims, damages and demands against the Secured Party arising out of the repossession, removal, retention or sale of the Collateral, unless due to the gross negligence or willful misconduct of the Secured Party.

(b) All ordinary costs and expenses incurred by the Secured Party in collection of the Obligations shall be borne exclusively by the Obligor including, without limitation, any costs, expenses, fees or disbursements incurred by outside agencies or attorneys retained by the Secured Party to effect collections of the Obligations or any Collateral securing the Obligations. The provisions of this paragraph shall not apply to any suits, actions, proceedings or claims of the nature referred to herein or otherwise which are based upon or related to the repayment of, or the taking of security for, any loans and/or advances made by the Secured Party to the Company that do not arise under the Letter Agreement or that are not participated in by the Secured Party, and the party making such loans and/or advances shall be exclusively responsible for such suits, actions, proceedings or claims and the payment of all such expenses in connection therewith.

8. **Costs and Expenses.** The Obligor agrees to pay all reasonable out-of-pocket fees, costs and expenses incurred in connection with any filing required hereunder, including without limitation, any financing statements, continuation statements, partial releases and/or termination statements related thereto or any expenses of any searches reasonably required by the Secured Party. The Obligor shall also pay all other claims and charges which in the reasonable opinion of the Secured Party might prejudice, imperil or otherwise affect the Collateral or the Security Interest therein. The Obligor will also, upon demand, pay to the Secured Party the amount of any and all reasonable expenses, including the reasonable fees and expenses of its counsel and of any experts and agents, which the Secured Party may incur in connection with (i) the enforcement of this Security Agreement, (ii) the custody or preservation of, or the sale of, collection from, or other realization upon, any of the Collateral, or (iii) the exercise or enforcement of any of the rights of the Secured Party under the Letter Agreement. Until so paid, any fees payable hereunder shall be added to the principal amount of the Note and shall bear interest at the Default Rate.

9. **Responsibility for Collateral.** The Obligor assumes all liabilities and responsibility in connection with all Collateral, and the obligations of the Obligor hereunder or under the Letter Agreement shall in no way be affected or diminished by reason of the loss, destruction, damage or theft of any of the Collateral or its unavailability for any reason.

10. **Security Interest Absolute.** All rights of the Secured Party and all Obligations of the Obligor hereunder, shall be absolute and unconditional, irrespective of: (a) any lack of validity or enforceability of this Security Agreement, the Letter Agreement, or any agreement entered into in connection with the foregoing, or any portion hereof or thereof; (b) any change in the time, manner or place of payment or performance of, or in any other term of, all or any of the Obligations, or any other amendment or waiver of or any consent to any departure from the Letter Agreement, or any other agreement entered into in connection with the foregoing; (c) any exchange, release or nonperfection of any of the Collateral, or any release or amendment or waiver of or consent to departure from any other collateral for, or any guaranty, or any other security, for all or any of the Obligations; (d) any action by the Secured Party to obtain, adjust, settle and cancel in its sole discretion any insurance claims or matters made or arising in connection with the Collateral; or (e) any other circumstance which might otherwise constitute any legal or equitable defense available to the Obligor, or a discharge of all or any part of the Security Interest granted hereby. Until the Obligations shall have been paid and performed in full, the rights of the Secured Party shall continue even if the Obligations are barred for any reason, including, without limitation, the running of the statute of limitations or bankruptcy. The Obligor expressly waives presentment, protest, notice of protest, demand, notice of nonpayment and demand for performance. In the event that at any time any transfer of any Collateral or any payment received by the Secured Party hereunder shall be deemed by final order of a court of competent jurisdiction to have been a voidable preference or fraudulent conveyance under the bankruptcy or insolvency laws of the United States, or shall be deemed to be otherwise due to any party other than the Secured Party, then, in any such event, the Obligor's obligations hereunder shall survive cancellation of this Security Agreement, and shall not be discharged or satisfied by any prior payment thereof and/or cancellation of this Security Agreement, but shall remain a valid and binding obligation enforceable in accordance with the terms and provisions hereof. The Obligor waives all right to require the Secured Party to proceed against any other person or to apply any Collateral which the Secured Party may hold at any time, or to marshal assets, or to pursue any other remedy. The Obligor waives any defense arising by reason of the application of the statute of limitations to any obligation secured hereby.

11. **Term of Agreement.** This Security Agreement and the Security Interest shall terminate on the repayment of all amounts due the Secured Party under the Letter Agreement and the Note. Upon such termination, the Secured Party, at the request and at the expense of the Obligor, will join in executing any termination statement with respect to any financing statement executed and filed pursuant to this Security Agreement.

12. **Power of Attorney; Further Assurances.**

(a) The Obligor authorizes the Secured Party, and does hereby make, constitute and appoint the Secured Party, and the Secured Party's officers, agents, successors or assigns with full power of substitution, as the Obligor's true and lawful attorney-in-fact, with power, in its own name or in the name of the Obligor, to, after the occurrence and during the continuance of an Event of Default, (i) endorse any debentures, checks, drafts, money orders, or other instruments of payment (including payments payable under or in respect of any policy of insurance) in respect of the Collateral that may come into possession of the Secured Party; (ii) to sign and endorse any UCC financing statement or any invoice, freight or express bill, bill of lading, storage or warehouse receipts, drafts against debtors, assignments, verifications and notices in connection with accounts, and other documents relating to the Collateral; (iii) to pay or discharge taxes, liens, security interests or other encumbrances at any time levied or placed on or threatened against the Collateral; (iv) to demand, collect, receipt for, compromise, settle and sue for monies due in respect of the Collateral; and (v) generally, to do, at the option of the Secured Party, and at the Obligor's expense, at any time, or from time to time, all acts and things which the Secured Party deems necessary to protect, preserve and realize upon the Collateral and the Security Interest granted therein in order to effect the intent of this Security Agreement and the Letter Agreement, all as fully and effectually as the Obligor might or could do; and the Obligor hereby ratifies all that said attorney shall lawfully do or cause to be done by virtue hereof. This power of attorney is coupled with an interest and shall be irrevocable for the term of this Security Agreement and thereafter as long as any of the Obligations shall be outstanding.

(b) On a continuing basis, the Obligor will make, execute, acknowledge, deliver, file and record, as the case may be, in the proper filing and recording places in any jurisdiction, including, without limitation, the jurisdictions indicated on **Schedule C**, attached hereto, all such instruments, and take all such action as may reasonably be deemed necessary or advisable, or as reasonably requested by the Secured Party, to perfect the Security Interest granted hereunder and otherwise to carry out the intent and purposes of this Security Agreement, or for assuring and confirming to the Secured Party the grant or perfection of a security interest in all the Collateral.

(c) The Obligor hereby irrevocably appoints the Secured Party as the Obligor's attorney-in-fact, with full authority in the place and stead of the Obligor and in the name of the Obligor, from time to time at the discretion of the Secured Party, to take any action and to execute any instrument which the Secured Party may deem necessary or advisable to accomplish the purposes of this Security Agreement, including the filing, in its sole discretion, of one or more financing or continuation statements and amendments thereto, relative to any of the Collateral without the signature of the Obligor where permitted by law.

13. **Notices.** All notices, requests, demands and other communications hereunder shall be in writing, with copies to all the other parties hereto, and shall be deemed to have been duly given when (i) if delivered by hand, upon receipt, (ii) if sent by facsimile, upon receipt of proof of sending thereof, (iii) if sent by nationally recognized overnight delivery service (receipt requested), the next business day or (iv) if mailed by first-class registered or certified mail, return receipt requested, postage prepaid, four days after posting in the U.S. mails, in each case if delivered to the following addresses:

If to the Obligor: to the address first set forth in the Preambles to this Security Agreement.

With copies to:

If to the Secured Party: to the address first set forth above.

With copies to:

14. **Other Security.** To the extent that the Obligations are now or hereafter secured by property other than the Collateral or by the guarantee, endorsement or property of any other person, firm, corporation or other entity, then the Secured Party shall have the right, in its sole discretion, to pursue, relinquish, subordinate, modify or take any other action with respect thereto, without in any way modifying or affecting any of the Secured Party's rights and remedies hereunder.

15. Miscellaneous.

(a) No course of dealing between the Obligor and the Secured Party, nor any failure to exercise, nor any delay in exercising, on the part of the Secured Party, any right, power or privilege hereunder or under the Letter Agreement shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or privilege hereunder or thereunder preclude any other or further exercise thereof or the exercise of any other right, power or privilege.

(b) All of the rights and remedies of the Secured Party with respect to the Collateral, whether established hereby or by the Letter Agreement or by any other agreements, instruments or documents or by law shall be cumulative and may be exercised singly or concurrently.

(c) This Security Agreement constitutes the entire agreement of the parties with respect to the subject matter hereof and is intended to supersede all prior negotiations, understandings and agreements with respect thereto. Except as specifically set forth in this Security Agreement, no provision of this Security Agreement may be modified or amended except by a written agreement specifically referring to this Security Agreement and signed by the parties hereto.

(d) In the event that any provision of this Security Agreement is held to be invalid, prohibited or unenforceable in any jurisdiction for any reason, unless such provision is narrowed by judicial construction, this Security Agreement shall, as to such jurisdiction, be construed as if such invalid, prohibited or unenforceable provision had been more narrowly drawn so as not to be invalid, prohibited or unenforceable. If, notwithstanding the foregoing, any provision of this Security Agreement is held to be invalid, prohibited or unenforceable in any jurisdiction, such provision, as to such jurisdiction, shall be ineffective to the extent of such invalidity, prohibition or unenforceability without invalidating the remaining portion of such provision or the other provisions of this Security Agreement and without affecting the validity or enforceability of such provision or the other provisions of this Security Agreement in any other jurisdiction.

(e) No waiver of any breach or default or any right under this Security Agreement shall be considered valid unless in writing and signed by the party giving such waiver, and no such waiver shall be deemed a waiver of any subsequent breach or default or right, whether of the same or similar nature or otherwise.

(f) This Security Agreement shall be binding upon and inure to the benefit of each party hereto and its successors and assigns.

(g) Each party shall take such further action and execute and deliver such further documents as may be necessary or appropriate in order to carry out the provisions and purposes of this Security Agreement.



(h) This Security Agreement shall be construed in accordance with the laws of the State of California, except to the extent the validity, perfection or enforcement of a security interest hereunder in respect of any particular Collateral which are governed by a jurisdiction other than the State of California in which case such law shall govern. Each of the parties hereto irrevocably submit to the exclusive jurisdiction of any California State or United States federal court sitting in Los Angeles county over any action or proceeding arising out of or relating to this Security Agreement, and the parties hereto hereby irrevocably agree that all claims in respect of such action or proceeding may be heard and determined in such California State or Federal court. The parties hereto agree that a final judgment in any such action or proceeding shall be conclusive and may be enforced in other jurisdictions by suit on the judgment or in any other manner provided by law. The parties hereto further waive any objection to venue in the State of California and any objection to an action or proceeding in the State of California on the basis of forum non conveniens.

(i) EACH PARTY HERETO HEREBY AGREES TO WAIVE ITS RESPECTIVE RIGHTS TO A JURY TRIAL OF ANY CLAIM OF CAUSE OF ACTION BASED UPON OR ARISING OUT OF THIS SECURITY AGREEMENT. THE SCOPE OF THIS WAIVER IS INTENDED TO BE ALL ENCOMPASSING OF ANY DISPUTES THAT MAY BE FILED IN ANY COURT AND THAT RELATE TO THE SUBJECT MATTER OF THIS SECURITY AGREEMENT, INCLUDING WITHOUT LIMITATION CONTRACT CLAIMS, TORT CLAIMS, BREACH OF DUTY CLAIMS AND ALL OTHER COMMON LAW AND STATUTORY CLAIMS. EACH PARTY HERETO ACKNOWLEDGES THAT THIS WAIVER IS A MATERIAL INDUCEMENT FOR EACH PARTY TO ENTER INTO A BUSINESS RELATIONSHIP, THAT EACH PARTY HAS ALREADY RELIED ON THIS WAIVER IN ENTERING INTO THIS SECURITY AGREEMENT AND THAT EACH PARTY WILL CONTINUE TO RELY ON THIS WAIVER IN THEIR RELATED FUTURE DEALINGS. EACH PARTY FURTHER WARRANTS AND REPRESENTS THAT IT HAS REVIEWED THIS WAIVER WITH ITS LEGAL COUNSEL, AND THAT SUCH PARTY HAS KNOWINGLY AND VOLUNTARILY WAIVED ITS RIGHTS TO A JURY TRIAL FOLLOWING SUCH CONSULTATION. THIS WAIVER IS IRREVOCABLE, MEANING THAT, NOTWITHSTANDING ANYTHING HEREIN TO THE CONTRARY, IT MAY NOT BE MODIFIED EITHER ORALLY OR IN WRITING, AND THIS WAIVER SHALL APPLY TO ANY SUBSEQUENT AMENDMENTS, RENEWALS AND SUPPLEMENTS OR MODIFICATIONS TO THIS SECURITY AGREEMENT. IN THE EVENT OF A LITIGATION, THIS SECURITY AGREEMENT MAY BE FILED AS A WRITTEN CONSENT TO A TRIAL BY THE COURT.

(j) This Security Agreement may be executed in any number of counterparts, each of which when so executed shall be deemed to be an original and, all of which taken together shall constitute one and the same Security Agreement. In the event that any signature is delivered by facsimile transmission, such signature shall create a valid binding obligation of the party executing (or on whose behalf such signature is executed) the same with the same force and effect as if such facsimile signature were the original thereof.

**[THE REMAINDER OF THIS PAGE IS LEFT BLANK INTENTIONALLY]**

IN WITNESS WHEREOF, the parties hereto have caused this Security Agreement to be duly executed on the day and year first above written.

**OBLIGOR:**

**TARGETED MEDICAL PHARMA, INC.**

By: /s/ William E. Shel  
Name: William E. Shell, MD  
Title: Chief Executive Officer

**SECURED PARTY:**

**AFH HOLDING AND ADVISORY, LLC**

By: /s/ Amir F. Heshmatpour  
Name: Amir F. Heshmatpour  
Title: Managing Director

**CERTIFICATION**  
Pursuant to 18 U.S.C. Section 1350,

As adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, William E. Shell, MD, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Targeted Medical Pharma, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Dated: August 14, 2012

Signature:           /s/ William E. Shell, MD  
                  William E. Shell, MD  
                  Principal Executive Officer

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**CERTIFICATION**  
Pursuant to 18 U.S.C. Section 1350,

As adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Ronald W. Rudolph certify that:

1. I have reviewed this quarterly report on Form 10-Q of Targeted Medical Pharma, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Dated: August 14, 2012

Signature:           /s/ Ronald W. Rudolph            
Ronald W. Rudolph  
Principal Financial Officer

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**CERTIFICATION**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  
(subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code), each of the undersigned officers of Targeted Medical Pharma, Inc., a Delaware corporation (the "Company"), does hereby certify, to such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended June 30, 2012 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 14, 2012

By: /s/ William E. Shell, MD

William E. Shell, MD  
Principal Executive Officer

By: /s/ Ronald W. Rudolph

Ronald W. Rudolph  
Principal Financial Officer

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