

Report of the Supervisory Board



Dr Walter Wenninger
Chairman of the Supervisory Board of PAION AG

Dear Shareholders,

During the past fiscal year, the Supervisory Board has performed its duties pursuant to the law, the company's articles of association and the by-laws and in fulfilment of its advisory and supervisory function has closely followed the business conduct of the Management Board. The Supervisory Board was directly involved in all decisions of major importance to the company. In the course of fulfilling its duties, the Supervisory Board has received regular, prompt and comprehensive written and verbal reports from the Management Board on PAION AG's corporate planning, the state and development of the company as well as all significant business transactions.

The Supervisory Board has carefully examined, discussed and voted on the decisions or measures of the Management Board that, pursuant to the law, the articles of association or the by-laws of the Management Board, require its approval as well as other decisions of fundamental importance. In addition to receiving its reports, I as Chairman of the Supervisory Board, have maintained regular contact with the Management Board, especially with the Chairman of the Management Board and the Chief Financial Officer, and I have kept myself informed of the current business development, in particular the progress of clinical studies and other essential business transactions.

Meetings of the Supervisory Board and focus of deliberations

The Supervisory Board held a total of eleven board meetings in the fiscal year 2009. The members attended six of these in person, while five meetings were conducted as joint conference calls. All meetings were collectively attended by the board members. In October 2009 an audit committee was established. All Supervisory Board members are members of the audit committee. Dr Spiekerkötter was appointed chairman of the audit committee. No further committees were established.

The Supervisory Board focused in its meetings in the fiscal year 2009 on the following subjects:

- The strategic positioning of the company
- The progress of the clinical studies with CNS 7056
- The situation regarding the search for a partner for CNS 7056 and M6G
- The development of all compounds
- The funding of the PAION group
- The adjustment of the compensation system for the Management Board from 2010 on with regard to new legal requirements (Adequacy of Management Board Remuneration Act (VorstAG), changes of the German Corporate Governance Code)
- The changes due to the German Act on the Modernisation of Accounting Law (BilMoG) and
- The cost reduction measures implemented at the beginning of 2009

The corporate budget adjustments for 2009 and the corporate budget planning for 2010, as developed by the Management Board were examined in detail and approved by the Supervisory Board. Based on mid- and long-term corporate planning as well as scenario comparisons the strategic orientation was discussed, reviewed and adjusted. The Supervisory Board has reviewed the information provided by the Management Board in detail and discussed it with the Management Board. Special attention was also paid to the risk situation and the risk management.

The Management Board kept the Supervisory Board regularly informed of the net assets, financial position and results of operations of the PAION group. The basis for this were the timely presented monthly, quarterly and annual financial reports as well as variance analyses.

The Supervisory Board and the audit committee respectively discussed the quarterly financial reports regularly before publication with the Management Board.

No conflicts of interest involving the members of the Supervisory Board, as set out in subsection 5.5 of the German Corporate Governance Code, arose in the financial year 2009.

The audit committee held two meetings since its establishment in October 2009 in the fiscal year 2009 and focused on the following subjects:

- The accounting of the company and the PAION group
- The valuation of assets, especially of the investments and the projects
- The monitoring of the effectiveness of the risk management system, the internal control system and the internal audit system
- The concept and plan of the Internal Audit
- The strategy of foreign exchange risk management

Corporate Governance

The concept of corporate governance stands for transparent business management that also aims to create long-term value. The Supervisory Board identifies itself with the principles of the German Corporate Governance Code. At the meeting of the Supervisory Board on 11 December 2009, the Supervisory Board and the Management Board released a joint and updated Declaration of Conformity in accordance with section 161 of the German Stock Corporation Act and subsequently made it permanently available to shareholders on the company's website at www.paion.com/corporategovernance. PAION AG complies with essentially all recommendations of the Government Commission German Corporate Governance Code, including those in the most recently amended version of 18 June 2009. An explanation of the few deviations from the Code as well as information on corporate governance at

PAION AG can be found in the Corporate Governance Report, jointly prepared by the Supervisory Board and the Management Board, which can be found on pages 18–22 of this annual report.

Financial statements and consolidated financial statements

Ernst & Young AG Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft, Cologne (following change of corporate form now: Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft, branch office Cologne) (“Ernst & Young”) was appointed auditor and group auditor for the financial year 2009 by the Annual General Meeting on 25 May 2009 and subsequently mandated to that effect by the Supervisory Board. In accordance with clause 7.2.1 of the German Corporate Governance Code, the independence of Ernst & Young was confirmed to us in writing prior to the Annual General Meeting. Ernst & Young has audited the financial statements and consolidated financial statements of PAION AG prepared by the Management Board, the management report and the group management report for the financial year 2009 and furnished them with an unqualified auditor's opinion. The group financial statements were drawn up in accordance with section 315 a of the German Commercial Code on the basis of the International Financial Reporting Standards (IFRS).

All members of the Supervisory Board received specific documentation relevant to the financial statements as well as the financial statements and the audit reports from the auditor well in advance of the meeting on 15 March 2010, where the financial statements were discussed. They studied these documents in detail in preparation for this meeting. At the meeting, the financial statements and consolidated financial statements were discussed in depth with the Management Board. The auditor also took part in this meeting. He reported on the audit, especially that no major weaknesses in the internal control systems and risk management systems with respect to the accounting process existed, commented on the focal points of the audit and was available to answer questions and provide supplementary information to the Supervisory Board.

The Supervisory Board acknowledges with approval the audit reports on the financial statements and consolidated financial statements as well as the management report and the consolidated management report. Following its own audit, the Supervisory Board does not raise objections and approves the financial statements and group financial statements prepared by the Management Board. The financial statements are therefore adopted.

Changes in the Management Board

Alexander Vos was a member of the Management Board until 7 September 2009 and left the company on 31 October 2009. The Supervisory Board would like to thank Mr Vos for his committed work in the interest of the company and wishes him all the best for the future.

The Supervisory Board thanks the members of the Management Board and all of the company's employees for their great commitment and for their achievements during the fiscal year 2009.

Aachen, March 2010

For the Supervisory Board



Dr Walter Wenninger

Chairman