

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549**

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2017

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 001-36385

BIOLASE, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction
of Incorporation or Organization)

87-0442441
(I.R.S. Employer
Identification No.)

4 Cromwell
Irvine, California 92618
(Address of Principal Executive Offices) (Zip code)

(949) 361-1200
(Registrant's Telephone Number, including Area Code)

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

Title of each class
Common Stock, par value \$0.001 per share

Name of each exchange on which registered
The NASDAQ Stock Market LLC
(NASDAQ Capital Market)

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

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

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

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

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the Registrant's common stock held by non-affiliates was \$34,143,958 based on the last sale price of common stock on June 30, 2017.

As of March 7, 2018, there were 102,344,682 shares of the registrant's common stock, par value \$0.001 per share, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement related to its 2018 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the registrant's fiscal year ended December 31, 2017, are incorporated by reference into Part III of this Annual Report on Form 10-K.

BIOLASE, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2017
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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K (“Form 10-K”), particularly in Item 1, “Business,” and Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and the documents incorporated by reference, includes “forward-looking statements” that involve risks and uncertainties, as well as assumptions that, if they prove incorrect or do not materialize as expected, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Examples of forward-looking statements include, but are not limited to any statements, predictions, or expectations regarding our strategy, future demand for improved dental care, compliance with laws and regulatory requirements, expenses, the impact of cost-saving measures, excise tax expenses, anticipated cash needs, capital requirements and capital expenditures, needs for additional financing, use of working capital, plans for future products and services and for enhancements of existing products and services, plans to explore potential collaborations, potential acquisitions of products and technologies, effects of engineering and development efforts, plans to expand our field sales force, the development of distributor relationships, anticipated growth strategies, ability to attract customers, the adequacy of our facilities, products and solutions from competitors, protection of patents and other technology, the ability of third party payers to pay for costs of our products, critical accounting policies and the impact of recent accounting pronouncements, recording tax benefits or other financial items in the future, plans, strategies, expectations, or objectives of management for future operations, our financial condition or prospects, and any other statement that is not historical fact. Forward-looking statements are often identified by the use of words such as “may,” “might,” “will,” “intend,” “should,” “could,” “can,” “would,” “continue,” “expect,” “believe,” “anticipate,” “estimate,” “predict,” “potential,” “plan,” “seek” and similar expressions.

These forward-looking statements are based on the expectations, estimates, projections, beliefs and assumptions of our management based on information available to management as of the date on which this Form 10-K was filed with the Securities and Exchange Commission (the “SEC”) or as of the date on which the information incorporated by reference was filed with the SEC, as applicable, all of which are subject to change. Forward-looking statements are subject to risks, uncertainties and other factors that are difficult to predict and could cause actual results to differ materially from those stated or implied by our forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to:

- global economic uncertainty and volatility in financial markets;
 - inability to raise additional capital on terms acceptable to us;
 - our relationships with, and the efforts of, third-party distributors;
 - our inability to overcome the hesitation of dentists and patients to adopt laser technologies;
 - failure in our efforts to train dental practitioners;
 - inconsistencies between future data and our clinical results;
 - competition from other companies, including those with greater resources;
 - our inability to successfully develop and commercialize enhanced or new products that remain competitive with products or alternative technologies developed by others;
 - the inability of our customers to obtain third-party reimbursement for their use of our products;
 - limitations on our ability to use net operating loss carryforwards;
 - problems in manufacturing our products;
 - warranty obligations if our products are defective;
 - adverse publicity regarding our technology or products;
 - adverse events to our patients during the use of our products, regardless of whether caused by our products;
 - failure of our suppliers to supply us with a sufficient amount or adequate quality of materials;
 - a change in suppliers, including our inability to purchase certain key components of our products from suppliers other than our current suppliers;
 - rapidly changing standards and competing technologies;
 - our inability to effectively manage and implement our growth strategies;
 - risks associated with operating in international markets, including potential liabilities under the Foreign Corrupt Practices Act (“FCPA”);
 - breaches of our information technology systems;
 - seasonality;
-

- litigation, including the failure of our insurance policies to cover certain expenses relating to litigation and our inability to reach a final settlement related to certain litigations;
- disruptions to our operations at our primary facility;
- loss of our key management personnel or our inability to attract or retain qualified personnel;
- risks and uncertainties relating to acquisitions, including difficulties integrating acquired businesses successfully into our existing operations and risks of discovering previously undisclosed liabilities;
- failure to comply with the reporting obligations of the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and Section 404 of the Sarbanes-Oxley Act of 2002, as amended (the “Sarbanes-Oxley Act”) or maintain adequate internal control over financial reporting;
- climate change initiatives;
- failure of our intellectual property rights to adequately protect our technologies;
- potential third-party claims that our products infringe their intellectual property rights;
- changes in government regulation or the inability to obtain or maintain necessary governmental approvals;
- our failure to comply with existing or new laws and regulations, including fraud and abuse and health information privacy and securities laws;
- changes in the regulatory requirements of the Food and Drug Administration (“FDA”) applicable to laser products, dental devices, or both;
- recall or other regulatory action concerning our products after receiving FDA clearance or approval;
- low trading volume of our common stock and high concentration of ownership;
- the volatility of our common stock; and
- our failure to comply with continued listing requirements of the NASDAQ Capital Market.

Further information about factors that could materially affect the Company, including our results of operations and financial condition, is contained under “Risk Factors” in Item 1A in this Form 10-K. Except as required by law, we undertake no obligation to revise or update any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, new information, or changes to future results over time or otherwise.

PART I

Item 1. *Business*

Overview

BIOLASE, Inc. (“BIOLASE” and, together with its consolidated subsidiaries, the “Company,” “we,” “our” or “us”) is a medical device company that develops, manufactures, markets, and sells laser systems in dentistry and medicine and also markets, sells, and distributes dental imaging equipment, including three-dimensional CAD/CAM intra-oral scanners and digital dentistry software. Our products advance the practice of dentistry and medicine for patients and health care professionals. Our proprietary dental laser systems allow dentists, periodontists, endodontists, oral surgeons, and other dental specialists to perform a broad range of minimally invasive dental procedures, including cosmetic, restorative, and complex surgical applications. Our laser systems are designed to provide clinically superior results for many types of dental procedures compared to those achieved with drills, scalpels, and other conventional instruments. We have clearance from the FDA to market and sell our laser systems in the United States and also have the necessary registration to market and sell our laser systems in Canada, the European Union, and many other countries outside the United States. Additionally, our in-licensed imaging equipment and related products improve diagnoses, applications, and procedures in dentistry and medicine.

We offer two categories of laser system products: Waterlase (all-tissue) systems and Diode (soft-tissue) systems. Our flagship brand, the Waterlase, uses a patented combination of water and laser energy to perform most procedures currently performed using drills, scalpels, and other traditional dental instruments for cutting soft and hard tissue. We also offer our Diode laser systems to perform soft tissue, pain therapy, and cosmetic procedures, including teeth whitening. We have approximately 220 issued and 95 pending U.S. and international patents, the majority of which are related to Waterlase technology. From 1998 through December 31, 2017, we sold over 36,200 laser systems in over 90 countries around the world. Contained in this total are approximately 12,400 Waterlase systems, including approximately 8,400 Waterlase MD, MDX, Express and iPlus systems. We were originally formed as Societe Endo Technic, SA (“SET”) in 1984 in Marseilles, France, to develop and market various endodontic and laser products. In 1987, SET merged into Pamplona Capital Corp., a public holding company incorporated in Delaware. In 1994, we changed our name to BIOLASE Technology, Inc. and in 2012, we changed our name to BIOLASE, Inc. Since 1998, we have been the global leading innovator, manufacturer, and marketer of dental laser systems.

We currently operate in a single reportable business segment. We had net revenues of \$46.9 million, \$51.8 million, and \$48.5 million, in 2017, 2016, and 2015, respectively, and we had net losses of \$16.9 million, \$15.4 million, and \$20.3 million for the same periods, respectively. We had assets of \$43.0 million and \$41.9 million as of December 31, 2017 and 2016, respectively.

Recent Developments

New Leadership Additions

Consistent with our goal to focus our energies on worldwide competitiveness, strengthening our leadership, and increasing the amount of attention we pay to our professional customers and their patients, we have made strategic personnel additions to our senior management team. In September 2017, we named Jonathan T. Lord, M.D. as our new Chairman of our board of directors (our “Board”). Dr. Lord has served on our Board since 2014 and also serves as Chairman of the Compensation Committee and a member of the Nominating and Corporate Governance Committee. He is a board-certified forensic pathologist and Fellow of the College of American Pathologists. Dr. Lord brings extensive innovation and executive management and board experience to his new role of Chairman. Effective October 1, 2017, we appointed John R. Beaver as our new Senior Vice President and Chief Financial Officer, who has proven leadership and technical experience in finance and business management in both public and private companies. Effective November 1, 2017, we appointed to our Board Richard B. Lanman, M.D., a well-known healthcare innovator and entrepreneur who specializes in the development and adoption of novel healthcare technologies. In January, we promoted from within a new Vice President of U.S.Sales, who has a wealth of experience and knowledge about our Company and the industry.

Rights Offering

We completed a rights offering on December 5, 2017 by selling 26,302,703 shares of our common stock. Gross proceeds were approximately \$12.0 million, and net proceeds, after offering expenses of approximately \$0.6 million, were approximately \$11.4 million. Certain affiliates of Larry Feinberg and an affiliate of Jack Schuler exercised their basic subscription rights and over-subscription privilege in the rights offering and purchased a total of 10,745,614 shares and 10,964,912 shares of our common stock, respectively, on the same terms as all other participants. We plan to use the net proceeds from the rights offering for our general working capital needs.

Industry Background

General

Dental procedures, including medical and cosmetic treatment, are performed on hard tissue, such as bone and teeth, and soft tissue, such as gum and other oral tissue.

The American Dental Association's ("ADA") last available Survey of Dental Services Rendered (the "ADA Study"), published in 2007, estimated that more than 200 million hard tissue procedures are performed annually in the United States. Hard tissue procedures include cavity preparation, root canals, and other procedures involving bone or teeth. Moreover, iData Research, an international market research group that specializes in medical device market dynamics, estimated that approximately 400 million hard tissue procedures are performed annually outside the United States.

The ADA also estimates that 46.5 million periodontal, implant, or soft tissue surgical procedures are performed annually in the United States. Periodontal procedures are performed on the supporting structures to remove periodontal and gum disease, which leads to tooth loss. Implant procedures include dental implant placement and restoration, and the treatment of peri-mucositis and peri-implantitis to mitigate implant failure, which is estimated to affect as many as 48% of all implants placed since 2000.

Furthermore, according to the ADA Study, over 90% of hard tissue procedures and 60% of periodontal, implants, and soft tissue, procedures in the United States are performed by general dentists. The remainder are performed by dental specialists, such as periodontists, pediatric dentists, implantologists, oral surgeons, prosthodontists, and endodontists. According to "Prevalence of Periodontitis in Adults in the United States" by Ede, Dye, Wei et al., recent evidence indicates that 47% of dental patients aged 30 or older have moderate to severe periodontitis that would benefit from intervention and Waterlase therapy. The ADA Health Policy Institute reported that in 2014, several key indicators of demand for dental services showed positive growth, including per capita dental expenditures, overall dental visits, and dentist earnings. The ADA Health Policy Institute also reported promising trends in patient access to health insurance coverage and increased consumerism of oral healthcare. Overall, the demand for dental services has continued to evolve positively due to population growth, aging demographics, and increased awareness of the benefits of preventive dentistry in reducing the incidence of oral and systemic disease. Periodontitis and peri-implantitis are two rapidly growing disease states requiring therapy in a dental practice.

According to "The Oral Health Atlas, 2nd edition," untreated tooth decay was the most prevalent of 291 oral disease conditions studied by the FDI World Dental Federation in 2015, with periodontal disease and associated complications being the 6th most prevalent oral disease state.

We believe there is a growing awareness among consumers globally of the value and importance of oral health and its connections to overall systemic health and wellness. Studies indicate a link between periodontitis and other health conditions such as heart disease, diabetes, and stroke. According to the 2013 Distribution of Dentists in the U.S. by Region and State, there were 177,625 active private practitioners in the U.S. According to the World Health Organization, there were 1.8 million dentists worldwide in 2012. As many developing nations continue to experience fiscal growth, we believe those nations will also experience higher demand for improved dental care. Corresponding growth resulting from dental practices competing for patients could create further demand for clinical solutions that enable dentists to perform minimally invasive dental procedures with less trauma, less anesthesia, improved patient acceptance, and clinically superior results. We believe our product offerings align with this trend.

Traditional Dental Instruments

Dentists and other specialists utilize a variety of instruments depending on the tissue involved and the type of procedure. Most procedures require the use of multiple instruments to achieve desired results. Many of the instruments available today are based on decades-old practices. Examples are as follows:

High-Speed Drills. Most dentists use conventional high-speed drills for hard tissue procedures, such as preparing cavities for filling, gaining access for performing root canals, and shaving or contouring oral bone tissue. Potentially adverse effects associated with drills include thermal heat transfer, vibration, pressure and noise. The cutting and grinding action of high-speed drills can cause damage, such as microfractures, to the patient's teeth. The trauma can lead to longer recovery times and the need for future crowns and root canals. Additionally, this grinding action of high-speed drills may weaken the tooth's underlying structure, leading to fractures and broken cusps. Procedures involving high-speed drills typically require anesthesia and are often the source of patient anxiety and fear. Because many dentists do not recommend anesthetizing more than one or two sections of the mouth in a single appointment, patients may need to return several times to complete their treatment plan.

Cutting Instruments. Soft tissue procedures are typically performed by oral surgeons or periodontists using scalpels, scissors, and other surgical tools. Due to the pain, bleeding, post-operative swelling, and discomfort associated with these instruments, most soft tissue procedures require the use of local anesthetic which may result in numbness and longer recovery time, and often require stitches. Bleeding can impair the practitioner's visibility during the procedure, thereby reducing efficiency and is a particular problem for patients with immune deficiencies or blood disorders and for patients taking blood-thinning medications.

Film Radiography Equipment. Dentists have traditionally relied on radiographic images produced by exposing photographic film to X-ray radiation as part of the examination and diagnosis of patients. These X-ray images can help reveal tooth decay, periodontal disease, bone loss, infections, hidden dental structures, abscesses or cysts, developmental abnormalities, some types of tumors, and other issues that might not be detected during a visual examination or upon probing with a handheld instrument. Due to the chemical development process required for film, however, this process is time-consuming, inefficient, costly for dental offices, and not environmentally friendly. Mistakes in the development process can require retakes which expose patients to additional radiation. Film X-rays also restrict the ability of doctors to enhance or further manipulate images for easier and more accurate analysis and treatment planning. Furthermore, one of the most critical limitations of film is that it is restricted to two-dimensional images, which can potentially lead to misdiagnosis.

Alternative Dental Instruments

Alternative technologies have been developed over the years to address the problems associated with traditional methods used in dentistry. However, most alternatives have addressed either hard or soft tissue applications but not both, or have other limitations.

Electrosurge Systems. Electrosurge systems use an electrical current to heat a shaped tip that simultaneously cuts and cauterizes soft tissue, resulting in less bleeding than occurs with scalpels. However, electrosurge systems are generally less precise than lasers and can damage surrounding tissue. Electrosurge systems are also not suitable for hard tissue procedures and, due to the depth of penetration, generally require anesthesia and a lengthy healing process. Electrosurge systems generally cannot be used in areas near metal fillings and dental implants. Finally, electrosurge systems generally cannot be used to treat patients with implanted pacemakers and defibrillators.

Traditional Laser Systems. More recently, lasers have gained acceptance for use in general and cosmetic dentistry. Most lasers used in dentistry have been adapted from other medical applications, such as dermatology, but are not optimally designed to perform common dental procedures. Most dental lasers use thermal energy to cut tissue and are used primarily for soft tissue procedures.

BIOLASE Products

Our laser systems and 3D CAD/CAM intraoral scanning and imaging solutions can provide dental professionals with enhanced capabilities for early diagnosis and minimally invasive treatment. Our product offering consists of the following:

Waterlase all-tissue laser systems. Our all-tissue Waterlase dental laser systems currently consist of the new Waterlase Express, our flagship Waterlase iPlus, and the Waterlase MD Turbo. Each of these systems features proprietary laser crystal technology that produces energy with specific absorption and tissue interaction characteristics specifically designed for dental procedures. It is minimally invasive and can precisely cut hard tissue, such as bone and teeth, and soft tissue, such as gums and skin, without the heat, vibration, bleeding, or pressure associated with traditional dental treatments. By combining the laser light and water, our Waterlase systems can eliminate the need for anesthesia in most cases and result in faster healing times compared to traditional methods of treatment, both of which could lead to improved patient-reported outcomes.

The Waterlase systems incorporate an ergonomic hand-piece and a user-friendly digital interface with clinical applications to control the mix of laser energy, air, and water, as well as the pulse rate. Each system also has been designed to be easily moved from operator to operator within a practice. We developed the Waterlase systems using internally developed intellectual property, as well as intellectual property obtained through various acquisitions. The Waterlase systems are FDA-cleared in the United States, CE mark-approved in Europe, and approved for sale in more than 90 other countries for dental uses. In the United States, we also have regulatory clearance for dermatological, aesthetic, and other general surgery uses.

Diode soft-tissue laser systems. Our Diode soft tissue laser systems currently consist of the Epic Pro, Epic X, Epic 10 and iLase diode lasers that perform soft tissue, hygiene, cosmetic procedures, teeth whitening, and provide temporary pain relief. Epic X, Epic 10, and iLase systems feature our proprietary 940nm wavelength and Epic Pro features our proprietary 940nm and 980nm wavelength with patented pulse technology called ComfortPulse, which is designed for added patient comfort. iLase was the first “personal” laser with no wires, footswitch, or cumbersome cables to manage. Epic 10 is a portable, powerful diode laser that facilitates clinical versatility with surgical, pain therapy, and whitening capabilities and provides an exceptional laser with an attractive value proposition. In December 2014, we introduced the Epic X diode laser, an enhanced soft tissue laser system featuring upgrades and improvements from our Epic 10. Epic Pro, released in 2016, is a soft-tissue diode laser with Super Thermal Pulse and Automatic Power Control features for enhanced patient comfort and clinical outcomes. The iLase, Epic X, Epic10, and Epic Pro are FDA-cleared in the United States, CE mark-approved in Europe, and approved for sale in more than 90 other countries for dental uses. In the United States, we also have regulatory clearance for dermatological, aesthetic, and other general surgery uses.

Imaging systems. Our imaging product line features a full line of 3Shape Trios intraoral scanners, digital impression systems and software for taking highly accurate 3D scans, which can be used to design crowns, study models, surgical guides for implant placement, and event orthodontic and athletic appliances. We distribute the 3Shape products under the manufacturer’s FDA 510(k) clearances.

Related Accessories and Consumable Products

We also manufacture and sell consumable products and accessories for our laser systems. Our Waterlase and Diode systems use disposable laser tips of differing sizes and shapes depending on the procedure being performed. We also market flexible fibers and hand pieces that dental practitioners replace at some point after initially purchasing laser systems. For our Epic systems, we sell teeth whitening gel kits.

BIOLASE Laser Solutions

Due to the limitations associated with traditional and alternative dental instruments, we believe there is a large market opportunity for all-tissue dental laser systems that provide superior clinical outcomes, reduce the need to use anesthesia, help reduce trauma, pain, and discomfort associated with dental procedures, and increase patient acceptance for treatment protocols. We also believe there is a large market opportunity for digital radiography systems that improve practice efficiency and accuracy of diagnosis, leading to superior treatment planning, increased practice revenue, and healthier outcomes for patients.

Our Waterlase systems precisely cut hard tissue, bone, and soft tissue with minimal or no damage to surrounding tissue and dental structures. Our Diode systems are designed to complement our Waterlase systems, and are used only in soft tissue procedures, pain therapy, hygiene, and cosmetic applications, including teeth whitening. The Diode systems, together with our Waterlase systems, offer practitioners a broad product line with a range of features and price points.

Benefits to Dental Professionals

- *Expanded range of procedures and revenue opportunities.* Our laser systems allow general dentists to perform surgical and cosmetic procedures that they are unable or unwilling to perform using conventional methods and that would typically be referred to a specialist. Our laser systems allow dentists to perform these procedures easily and efficiently, increasing their range of skills, professional and patient satisfaction levels, patient retention rates, new patient attraction rates, and revenues.
- *Additional procedures through increased information and efficiency.* Our laser systems can shorten and reduce the number of patient visits, providing dental professionals with the ability to service more patients. For hard tissue procedures, our Waterlase systems can reduce the need for anesthesia, which enables the dental practitioner to perform multiple procedures in one visit. The Waterlase and Diode systems cut soft tissue more precisely and with minimal bleeding when compared to traditional tools such as scalpels and electrosurge systems. We have FDA clearance for treatment indications for use that comprise our REPAIR Perio and REPAIR Implant, our proprietary periodontal protocols for subgingival calculus removal and debridement of root surfaces and implant surfaces using the Waterlase system and patented Radial Firing Perio Tips. This is a minimally invasive treatment for moderate to advanced gum and peri-implant diseases, which are among the leading causes of dental health conditions for adults over age 35 and conditions that impact more than half of Americans over the age of 55. In addition, our Epic system can be used to quickly perform in-office teeth whitening with our proprietary whitening gel and to provide temporary pain relief. Our digital imaging systems allow dentists to diagnose and discover cases that they might not be able to detect with film images or other two-dimensional images, thereby giving them the ability to offer more treatment options for patients.

- *Increased loyalty and expanded patient base.* We believe the improved patient comfort and convenience offered by our laser systems, the reduction in chair time and radiation exposure of our digital imaging systems, and the benefits of in-office, chair-side milling helps improve patient retention rates, attract new patients, and increase revenue per patient, demand for elective procedures, acceptance of treatment plans, and word-of-mouth referrals.
- *Improved clinical outcomes.* Our laser systems can be used for dozens of clinical indications with reduced trauma, swelling, and general discomfort of the patient, resulting in improved clinical outcomes and less follow-up treatment. In parallel, our digital imaging systems provide greater clarity and information, making it possible for the doctor to determine the optimal diagnosis and treatment plan. Our products collectively improve clinical outcomes, making it possible for practitioners to devote time to new cases, rather than managing or treating complications.

Benefits to Patients

- *Comfort.* Our Waterlase systems allow dentists to perform minimally invasive dental procedures without anesthesia in many cases, and patients recover more comfortably, faster, and with less pain than when treated with conventional instruments. The heat, vibration, microfractures, trauma, or pressure associated with traditional dental methods are largely avoided.
- *Convenience and efficiency.* Procedures utilizing our Waterlase systems do not require anesthesia in many cases, which allows dental practitioners to perform multiple procedures in one appointment, which saves patients time. Digital images are available almost immediately, so patients do not have to spend extra time in the dental chair waiting for film to be developed.
- *Reduced trauma.* Waterlase systems allow for a faster and more pleasant patient recovery with less swelling, bleeding, and general discomfort than when treated with conventional instruments.
- *Broader range of available procedures.* Due to the comfort and convenience of procedures utilizing our Waterlase system, patients may be more likely to consider cosmetic and other elective procedures resulting in better smiles and oral health. Our Waterlase system received expanded clearance from the FDA for dermatological, aesthetic, and general surgery uses, as well as dental procedures. Since digital images are displayed on computer monitors, doctors can make treatment planning a more personal experience for patients. We believe that these factors will lead to greater patient case acceptance.

Business Strategy

Our business strategy includes the following key elements:

- *Increasing awareness of and demand for our products among dental practitioners.* We intend to increase demand for our products by educating dental practitioners and patients about the clinical benefits of our product suite. We plan to continue participation in key industry trade shows, the World Clinical Laser Institute® (“WCLI®”) (which we founded in 2002), dental schools, and other educational forums. Our products are also used for clinical research, which often leads to published articles that can garner attention from dental practitioners.
- *Increasing awareness and education in laser dentistry.* We added local specialists to our staff in southern California to offer dentists more support in maximizing the use of their lasers. In addition, we plan to offer more educational courses, informational events and community activities to help ensure that dentists and their patients are provided with the latest information in laser dentistry. We have developed a local advisory board of dentistry veterans whose collective expertise should serve as an excellent resource that will help propel the local market forward.
- *Increasing awareness of and demand for our laser systems among patients.* We also intend to increase demand for our products by educating patients about the clinical benefits of the Waterlase and Diode systems. We believe that patients will understand the clinical benefits and seek out dental practitioners that offer the Waterlase and Diode systems, which, in turn, will result in increased demand for our systems from dental practitioners.
- *Strengthening customer training and clinical education.* We provide introductory, advanced, and specialized training for dental practitioners to increase their proficiency and to certify them. Our goal is to provide our customers world class training that is accessible and can be executed with a practical technique.

- *Strengthening sales and distribution capabilities.* In the U.S. and Canada, we primarily distribute our products directly to dental practitioners via our field sales force. During 2016, we augmented our field sales force efforts with outbound, phone-based sales support initiatives. These initiatives are driven from our corporate headquarters and are comprised of sales representatives and lead generators working in partnership with the field sales team to maximize effectiveness in engaging and servicing customers. In addition to our field sales force in North America, we also use various independent distributors to sell and support our products throughout Europe, the Middle East, Latin America, and Asia-Pacific regions. We plan to continue to build out the infrastructure to support our customers and to drive revenue and profit growth, both domestically and internationally. This includes expanding our sales presence with respect to the rapidly growing group practices, group purchasing organizations, and government channels.
- *Improving product quality.* We plan to achieve the industry's highest rate of defect-free delivery of products, maintain high quality standards, and address and timely resolve customer complaints. In the U.S., we provide maintenance and support services to customers through our support hotline and dedicated staff of in-house and field service personnel. Outside the U.S., we maintain a network of factory-certified service technicians to provide maintenance and support services to customers.
- *Strengthening and defending technology leadership.* We plan to continue protecting our intellectual property rights by expanding our existing patent portfolio in the United States and internationally. We strategically enforce our intellectual property rights worldwide.
- *Expanding our product portfolio to dental practitioners.* By combining our Waterlase and Epic laser systems with select, in-line digital imaging, intra-oral scanners, CAD/CAM design, and chairside milling products, dental offices can accurately and timely address unmet patient needs with convenience. We plan to continue to evaluate how to optimize the manner in which we market and sell additional products to supplement our core Waterlase and Epic franchises.
- *Creating value through innovation and leveraging existing technologies into adjacent medical applications.* We plan to expand our product line and clinical applications by developing enhancements and transformational innovations, including new clinical solutions for dental applications and for other adjacent medical applications. In particular, we believe that our existing technologies can provide significant improvements over existing standards of care in fields, including ophthalmology, otolaryngology, orthopedics, podiatry, pain management, aesthetics/dermatology, veterinary, and consumer products. We plan to continue to explore potential collaborations to bring our proprietary laser technologies with expanded FDA-cleared indications for other medical applications in the future. In addition, we may acquire complementary products and technologies. We also aim to increase our consumables revenue by selling more single-use accessories used by dental practitioners when performing procedures using our dental laser systems.

Warranties

Our Waterlase laser systems sold domestically are covered by a warranty against defects in material and workmanship for a period of up to one year from the date of sale to the end-user by us or a distributor. Our Diode systems sold domestically are covered by a warranty against defects in material and workmanship for a period of up to two years from the date of sale to the end-user by us or a distributor. Waterlase systems and Diode systems sold internationally are covered by a warranty against defects in material and workmanship for a period of up to 28 months from date of sale to the international distributor. Our laser systems warranty covers parts and service for sales in our North American territories and parts only for international distributor sales. In North America and select international locations, we sell extended warranty contracts to our laser systems end users that cover the period after the expiration of our standard warranty coverage for our laser systems. Extended warranty coverage provided under our service contracts varies by the type of system and the level of service desired by the customer. Products or accessories remanufactured, refurbished, or sold by unauthorized parties, voids all warranties in place for such products and exempts us from liability issues relating to the use of such products. We distribute extended warranties on certain imaging products, including our digital radiography products. However, all imaging products that we distribute are initially covered by manufacturer's warranties.

Manufacturing

Our strategy is to manufacture products in-house when it is efficient for us to do so. We currently manufacture, assemble, and test all of our laser systems at our corporate headquarters facility in Irvine, California. The 57,000 square foot facility has approximately 20,000 square feet dedicated to manufacturing and warehousing. The facility is ISO 13485 certified. ISO 13485 certification provides guidelines for our quality management system associated with the design, manufacture, installation, and servicing of our products. In addition, our U.S. facility is registered with the FDA and complies in all material respects with the FDA's Quality System Regulation.

We use an integrated approach to manufacturing, including the assembly of tips, laser hand pieces, fiber assemblies, laser heads, electro-mechanical subassembly, final assembly, and testing. We obtain components and subassemblies for our products from third-party suppliers, the majority of which are located in the United States. We generally purchase components and subassemblies from a limited group of suppliers through purchase orders. In general, we rely on these purchase orders and do not have written supply contracts with many of our key suppliers. Three key components used in our Waterlase system (power suppliers, laser crystals, and fiber components) are each supplied by separate single-source suppliers. In recent years, we have not experienced material delays from the suppliers of these three key components. However, an unexpected interruption from a single-source supplier could cause manufacturing delays, re-engineering, significant costs, and sales disruptions, any of which could have a material adverse effect on our operations. As of the date on which this Form 10-K was filed with the SEC, we were in the process of identifying and qualifying alternate source suppliers for our key components, including but not limited to those noted above. There can be no assurance, however, that we will successfully identify and qualify an alternate source supplier for any of our key components or that we could enter into an agreement with any such alternate source supplier on terms acceptable to us.

As discussed below, we are subject to periodic inspections by the FDA as a manufacturer of medical devices. Such inspections can cover manufacturing, design, production, reporting, recordkeeping, and other processes and can lead to FDA observations requiring corrective action, which can disrupt normal processes.

Marketing and Sales

Marketing

We market our laser systems worldwide. Our marketing efforts are focused on driving brand awareness and demand for BIOLASE laser solutions with dental practitioners. We also continue to test methods to increase awareness of our brands' benefits by marketing directly to patients.

Dental Practitioners. We market our laser systems to dental practitioners through regional, national, and international educational events, seminars, industry tradeshows, trade publications, digital/social media, field sales forces (in North America, Canada, and Germany), and agents and distributors. We also use brochures, direct communications, public relations, and other promotional tools and materials.

Our primary marketing message to dental practitioners focuses on the ability of BIOLASE lasers to resolve dental challenges and deliver improved cash flow and return on investment ("ROF"), which can be realized with improved patient-reported outcomes. Our World Clinical Laser Institute (the "WCLI") is a leader in educating and training dental practitioners in laser dentistry. We believe that, as the community of BIOLASE dental practitioners expands, the WCLI will continue to deliver fresh and exciting laser educational opportunities utilizing the latest in learning methodologies and platforms. The WCLI conducts and sponsors educational programs domestically and internationally for dental practitioners, researchers, and academicians, including one, two, and three-day seminars and training sessions involving in-depth presentations on the use of lasers in dentistry. In addition, we have developed relationships with research institutions, dental schools, and dental laboratories that use our products for clinical research and in-clinical training. We believe these relationships will continue to increase awareness of and demand for our products.

Patients. We plan to continue to test ways to effectively market the benefits of our laser systems directly to patients through marketing and advertising programs, including the internet, search engine optimization, social media, print and broadcast media, and point-of-sale materials in dental practitioners' offices. We believe that making patients aware of our laser systems and their benefits will motivate them to request from dental practitioners laser procedures and their outcomes thereby increasing demand for our brands. We can be found online at biolase.com, and on Facebook, Twitter, LinkedIn, and Vimeo. Unless specifically stated otherwise, none of the information contained on any of these sites online is incorporated in this Form 10-K by reference.

Sales

We sell our products primarily to dentists in general practice through our field sales force and our distributor network. We expect our laser systems to continue to gain acceptance among periodontists, endodontists, oral surgeons, pediatric dentists, and other dental specialists as they become aware of the clinical benefits and minimally invasive treatment options available by using our laser systems.

The following table summarizes our net revenues by category for the years ended December 31, 2017, 2016, and 2015 (dollars in thousands):

	Years Ended December 31,					
	2017		2016		2015	
Laser systems	\$ 29,121	62.0%	\$ 35,150	67.9%	\$ 32,691	67.5%
Imaging systems	3,685	7.9%	3,066	5.9%	2,237	4.6%
Consumables and other	7,332	15.6%	6,906	13.3%	6,877	14.2%
Services revenue	6,660	14.2%	6,539	12.6%	6,465	13.3%
Products and services revenue	46,798	99.7%	51,661	99.7%	48,270	99.6%
License fees and royalties	128	0.3%	149	0.3%	205	0.4%
Net revenue	<u>\$ 46,926</u>	<u>100.0%</u>	<u>\$ 51,810</u>	<u>100.0%</u>	<u>\$ 48,475</u>	<u>100.0%</u>

Net revenue by geographic location based on the location of customers was as follows (in thousands):

	Years Ended December 31,		
	2017	2016	2015
United States	\$ 29,296	\$ 33,385	\$ 29,433
International	17,630	18,425	19,042
	<u>\$ 46,926</u>	<u>\$ 51,810</u>	<u>\$ 48,475</u>

International revenue accounts for a significant portion of our total revenue and accounted for approximately 38%, 36%, and 39% of our net revenue in 2017, 2016, and 2015, respectively. No individual country outside the United States represented more than 10% of our net revenue during the years ended December 31, 2017, 2016, and 2015.

For financial information about our long-lived assets, see Note 2 and Note 9 to the *Notes to the Consolidated Financial Statements — Summary of Significant Accounting Policies* and — *Segment Information*.

North American Sales. In the United States and Canada, we primarily sell our products directly to dental practitioners utilizing a field sales force consisting of laser sales representatives and regional managers. We also have an in-house sales force, which is located at our corporate headquarters and is comprised of sales representatives and lead generators who work in partnership with the field sales team to maximize sales by leveraging the existing installed customer base.

International Sales. Our distributors purchase laser systems and disposables from us at wholesale dealer prices and resell them to dentists in their sales territories. All sales to distributors are final, and we can terminate our arrangements with dealers, agents, and distributors for cause or non-performance. We have granted certain distributors the right to be our exclusive distributor in select territories. These distributors are generally required to satisfy certain minimum purchase requirements to maintain their exclusivity. We have sold our products directly to end users in Germany since 2011 and directly to end users in India and neighboring countries since 2012.

Customer Concentration. We sell our products through our field sales force, agents, and distributors. For the years ended December 31, 2017, 2016, and 2015, sales to our largest distributor worldwide accounted for approximately 4%, 4%, and 3%, respectively, of our net revenue.

Customer Service. We provide high quality maintenance and support services in the United States through our support hotline and dedicated staff of in-house and field service personnel. Outside the United States, we maintain a network of factory-certified service technicians to provide maintenance and support services to customers. Our international distributors are responsible for providing maintenance and support services for products sold by them. We provide parts to distributors at no additional charge for products covered under warranty.

Financing Options. Most customers (other than distributors) finance their purchases through several third-party financial institutions with which we have established good relationships. In the United States and Canada, third-party customers enter into a financing agreement with one of the financial institutions that purchases the product from us or one of our distributors. We are not party to these financing agreements. Thus, if the customer agrees to pay the financial institution in installments, we do not bear the credit risk. The financial institutions do not have recourse to us for a customer's failure to make payments, nor do we have any obligation to take back the product.

Seasonality. Typically, we experience fluctuations in revenue from quarter to quarter due to seasonality. Revenue in the first quarter typically is lower than average and revenue in the fourth quarter typically is higher than average due to the buying patterns of dental practitioners. We believe that this trend exists because a significant number of dentists purchase their capital equipment towards the end of the calendar year to maximize their practice earnings while seeking to minimize their taxes. They often use certain tax incentives, such as accelerated depreciation methods for purchasing capital equipment, as part of their year-end tax planning. In addition, revenue in the third quarter may be affected by vacation patterns which can cause revenue to be flat or lower than in the second quarter of the year. Our historical seasonal fluctuations may also be impacted by sales promotions used by large dental distributors that encourage end-of-quarter and end-of-year buying in our industry. Because of these seasonal fluctuations, historically we have often used less cash in operations for the six months ended December 31 as compared to the six months ended June 30.

Engineering and Product Development

Engineering and product development activities are essential to maintaining and enhancing our business. We believe our engineering and product development team has demonstrated its ability to develop innovative products that meet evolving market needs. Our engineering and product development group consists of 20 individuals with medical device and laser development experience, including two Ph.Ds. During the years ended December 31, 2017, 2016, and 2015, our engineering and product development expenses totaled approximately \$6.2 million, \$7.8 million, and \$7.3 million, respectively. Our current engineering and product development activities are focused on developing new product platforms, improving our existing products and technology and extending our product range in order to provide dental practitioners and patients with new and improved protocols or procedures that are less painful and have clinically superior results. Some examples of the improvements we are pursuing for our laser systems include faster cutting speed, improved ease of use, less need for anesthesia, interconnectivity, and an expanded portfolio of consumable products for use with our laser systems. Our engineering and product development activities encompass both fundamental and applied fields. We seek to improve methods to perform clinical procedures through the use of new laser wavelengths, laser operation modes and accessories.

We also devote engineering and product development resources toward markets outside of dentistry in which we might exploit our technology platform and capabilities. We believe our laser technology and development capabilities could address unmet needs in several other medical applications, including ophthalmology, otolaryngology, orthopedics, podiatry, pain management, aesthetics/dermatology, veterinary, and consumer products. We have already started to enter the otolaryngology, pain management, and veterinary markets to varying degrees.

To further our development efforts, we have entered into a development and distribution agreement with IPG Medical. The development and distribution agreement between the Company and IPG covers several projects in various stages of development, with the expectation that these projects will culminate in commercialized joint dental laser products, accessories, or integral system components. The parties will collaborate in the design and development of these new products and applications, with each party contributing its technological expertise, know-how, and development resources. We will be responsible for U.S. and international registrations of all dental products resulting from the agreement, and we will have exclusive worldwide commercial distribution rights for certain products over a multi-year initial term after completion of development.

Intellectual Property and Proprietary Rights

We believe that to maintain a competitive advantage in the marketplace, we must develop and maintain protection of the proprietary aspects of our technology. We rely on a combination of patents, trademarks, trade secrets, copyrights and other intellectual property rights to protect our intellectual property. We have developed a patent portfolio internally, and to a lesser extent through acquisitions and licensing, that covers many aspects of our product offerings. As of December 31, 2017, we had approximately 220 issued patents and 95 pending patent applications in the United States, Europe and other countries. While we hold a variety of patents that cover a broad range of technologies and methods, the majority of these patents provide market protection for our core technologies incorporated in our laser systems and related accessories. Existing patents related to our core technology, which are at various stages of being incorporated into our products, are scheduled to expire as follows: 11 in 2018 and 2 in 2019, with the majority having expiration dates ranging from 2025 to 2038. With approximately 95 patent applications pending, we expect the number of new grants to exceed the number of patents expiring. We do not expect the expiration of the expired or soon-to-expire patents to have a material adverse effect on our business, financial condition, or results of operations.

There are risks related to our intellectual property rights. For further details on these risks, see Item 1A — “Risk Factors.”

Competition

We operate under relatively competitive market conditions. We believe that the principal competitive factors for companies that market technologies in dental and other medical applications include acceptance by leading dental and medical practitioners, product performance, product pricing, intellectual property protection, customer education and support, timing of new product research, and development of successful national and international distribution channels.

Our competitors vary by product and location. There are companies that market some, but not all, of the same types of products as ours. Our laser systems compete with other lasers, mostly with other wavelengths, patient outcomes, and benefit profiles, as well as with drills, scalpels, scissors, air abrasion systems, and a variety of other tools that are used to perform dental and medical procedures. We believe our products have key differentiating performance features. For example, we market diode lasers which also have FDA clearance for use in both pain management therapy and teeth whitening and our Waterlase systems have been FDA-cleared for a wide range of uses beyond dentistry, including dermatological, aesthetics, and other general surgery uses. Our teeth whitening technology competes with other in-office whitening products and high intensity lights used by dentists, as well as teeth whitening strips, and other over-the-counter products. Our pain management technology competes with a variety of traditional, advanced, and pharmaceutical pain management products and services. The dental imaging equipment and in-office milling machines that we offer compete with traditional dental laboratories, imaging centers and products and services.

Traditional tools are generally less expensive than our laser systems for performing similar procedures. For example, a high-speed drill or an electro surge device can be purchased for less than \$2,500. In addition, though our systems are superior to traditional tools in many ways, they are not intended to replace all of the applications of traditional tools, such as removing metal fillings and certain polishing and grinding functions.

Some of our competitors have significantly greater financial, marketing, and/or technical resources than we do. In addition, some competitors have developed, and others may attempt to develop, products with applications similar to those performed by our products. Because of the large size of the potential market for our products, it is possible that new or existing competitors may develop competing products, procedures, or clinical solutions that could prove to be more effective, safer, or less costly than procedures using our laser systems. The introduction of new products, procedures, or clinical solutions by competitors may result in price reductions, reduced margins, or loss of market share, or may render our products obsolete.

Government Regulations

FDA and Related Regulatory Requirements

Our products are subject to extensive regulation particularly as to safety, efficacy, and adherence to FDA Quality System Regulation and related manufacturing standards. Medical device products are subject to rigorous FDA and other governmental agency regulations in the United States and similar regulations of foreign agencies abroad. The FDA regulates the design, development, research, preclinical and clinical testing, introduction, manufacture, advertising, labeling, packaging, marketing, distribution, import and export, and record keeping for such products, in order to ensure that medical products distributed in the United States are safe and effective for their intended use. In addition, the FDA is authorized to establish special controls to provide reasonable assurance of the safety and effectiveness of most devices. Non-compliance with applicable requirements can result in import detentions, fines, civil and administrative penalties, injunctions, suspensions or losses of regulatory approvals, recall or seizure of products, operating restrictions, refusal of the government to approve product export applications or allow us to enter into supply contracts, and criminal prosecution.

Unless an exemption applies, the FDA requires that a manufacturer introducing a new medical device or a new indication for use of an existing medical device obtain either a Section 510(k) premarket notification clearance or a premarket approval ("PMA") before introducing it into the U.S. market. The type of marketing authorization is generally linked to the classification of the device. The FDA classifies medical devices into one of three classes (Class I, II, or III) based on the degree of risk the FDA determines to be associated with a device and the level of regulatory control deemed necessary to ensure the device's safety and effectiveness.

Our products currently marketed in the United States are marketed pursuant to 510(k) pre-marketing clearances and are either Class I, Class II, or Class III devices. The process of obtaining a Section 510(k) clearance generally requires the submission of performance data and often clinical data, which in some cases can be extensive, to demonstrate that the device is "substantially equivalent" to a device that was on the market before 1976 or to a device that has been found by the FDA to be "substantially equivalent" to such a pre-1976 device (referred to as "predicate device"). As a result, FDA clearance requirements may extend the development process for a considerable length of time. In addition, in some cases, the FDA may require additional review by an advisory panel, which can further lengthen the process. The PMA process, which is reserved for new devices that are not substantially equivalent to any predicate device and for high-risk devices or those that are used to support or sustain human life, may take several years and requires the submission of extensive performance and clinical information.

Medical devices can be marketed only for the indications for which they are cleared or approved. After a device has received 510(k) clearance for a specific intended use, any change or modification that significantly affects its safety or effectiveness, such as a significant change in the design, materials, method of manufacture, or intended use, may require a new 510(k) clearance or PMA approval and payment of an FDA user fee. The determination as to whether or not a modification could significantly affect the device's safety or effectiveness is initially left to the manufacturer using available FDA guidance; however, the FDA may review this determination to evaluate the regulatory status of the modified product at any time and may require the manufacturer to cease marketing and recall the modified device until 510(k) clearance or PMA approval is obtained. The manufacturer may also be subject to significant regulatory fines or penalties.

Any devices we manufacture and distribute pursuant to clearance or approval by the FDA are subject to extensive and continuing regulation by the FDA and certain state agencies. These include product listing and establishment registration requirements, which help facilitate FDA inspections and other regulatory actions. As a medical device manufacturer, all of our manufacturing facilities are subject to inspection on a routine basis by the FDA. We are required to adhere to applicable regulations setting forth detailed current good manufacturing practice ("cGMP") requirements, as set forth in the FDA's Quality System Regulation ("QSR"), which require manufacturers, including third-party manufacturers, to follow stringent design, testing, control, documentation and other quality assurance procedures during all phases of the design and manufacturing process. Noncompliance with these standards can result in, among other things, fines, injunctions, civil penalties, recalls or seizures of products, total or partial suspension of production, refusal of the government to grant 510(k) clearance or PMA approval of devices, withdrawal of marketing approvals, and criminal prosecutions. We believe that our design, manufacturing, and quality control procedures are in compliance with the FDA's regulatory requirements.

We must also comply with post-market surveillance regulations, including medical device reporting requirements which require that we review and report to the FDA any incident in which our products may have caused or contributed to a death or serious injury. We must also report any incident in which any of our products has malfunctioned if that malfunction would likely cause or contribute to a death or serious injury if it were to recur.

Labeling and promotional activities are subject to scrutiny by the FDA and, in certain circumstances, by the Federal Trade Commission ("FTC") and by state regulatory and enforcement authorities. Medical devices approved or cleared by the FDA may not be promoted for unapproved or uncleared uses, otherwise known as "off-label" promotion. The FDA and other agencies actively enforce the laws and regulations prohibiting the promotion of off-label uses, and a company that is found to have improperly promoted off-label uses may be subject to significant liability, including substantial monetary penalties and criminal prosecution.

Promotional activities for FDA-regulated products of other companies have also been the subject of enforcement actions brought under health care reimbursement laws and consumer protection statutes. In addition, under the federal Lanham Act and similar state laws, competitors and others can initiate litigation relating to advertising claims. If the FDA determines that our promotional materials or training constitutes promotion of an uncleared or unapproved use, the FDA could request that we modify our training or promotional materials or subject us to regulatory or enforcement actions, including the issuance of an untitled letter, a notice of violation, a warning letter, an injunction, a seizure, a civil fine, or criminal penalties. In that event, our reputation could be damaged and adoption of the products could be impaired.

We have registered with the FDA as a medical device manufacturer and we have obtained a manufacturing license from the California Department of Health Services. As a manufacturer, we are subject to announced and unannounced facility inspections by the FDA and the California Department of Health Services to determine our compliance with various regulations. Our subcontractors' manufacturing facilities are also subject to inspection.

Foreign Regulation

Sales of medical devices outside the United States are subject to regulatory requirements that vary widely from country to country. In the EU, placing our medical devices on the market must comply with the requirements of Council Directive 93/42/EEC concerning medical devices ("MDD"). Applicable requirements include compliance with the essential requirements of the MDD (the "Essential Requirements") and the CE marking process. Our devices are classified as Class I, Class IIa, Class IIb or Class III devices.

Medical devices marketed in the EU must meet all proper regulatory requirements and have a CE marking affixed to them. For devices falling within Class I (low risk), the manufacturer is responsible for ensuring that the product complies with the Essential Requirements and must draw up a written statement to this effect (a "Declaration of Conformity"). Class I devices without a measuring function and supplied in non-sterile condition do not require the involvement of an organization designated by an EU-competent authority to assess the conformity of certain products before being placed on the EU market (a "Notified Body").

Manufacturers of sterile products and devices with a measuring function must apply to a Notified Body for certification of the aspects of manufacture relating to sterility or metrology.

For devices falling within Class IIa (low – medium risk), in order to affix the CE marking and place the product on the EU market, the manufacturer must follow one of several authorization procedures involving the engagement of a Notified Body. For Class I devices, the manufacturer is responsible for declaring conformity with the provisions of the MDD and ensuring that the products comply with the Essential Requirements. This declaration must be supported by a conformity assessment by a Notified Body. Once the manufacturer has received certification from the Notified Body and issued a Declaration of Conformity, it may affix the CE marking to the relevant products and place them on the EU market.

For devices falling within Class IIb (medium – high risk) and Class III (high risk), in order to affix the CE marking and place the product on the EU market, the manufacturer must follow one of several authorization procedures. For Class IIa devices, this requires the engagement of a Notified Body. The procedure for placing Class III devices on the market is similar to that applicable for Class IIb devices. However, the manufacturer must also submit a design dossier to the Notified Body for approval under Annex II of the MDD, and some of the authorization procedures permitted for Class IIb devices are not permitted.

Once medical devices correctly have a CE marking and comply with other applicable regulatory requirements, they may be placed on the market in any member state of the European Economic Area (“EEA”). However, a CE marking does not indicate that the manufacturer’s quality system or that a product’s safety profile has been approved or assessed by competent authority.

In addition, other EU regulatory requirements may apply to our medical devices, including other types of CE markings having different requirements, where applicable. For example, Directive 2014/35/EU relating to the making available on the market of electrical equipment designed for use within certain voltage limits, Directive 2014/30/EU on electromagnetic compatibility and Directive 2011/65/EU on the restriction of the use of certain hazardous substances in electrical and electronic equipment may apply to our electrical products. Moreover, we must ensure compliance with applicable EU chemical legislation such as Directive 2011/65/EU on the restriction of the use of certain hazardous substances in electrical and electronic equipment and Regulation 1907/2006 on the Registration, Evaluation, Authorization and Restriction of Chemicals. Additional EU requirements may also include safety, health, and environmental protection.

The European Association for the Co-ordination of Consumer Representation in Standardization has cautioned that, amongst other things, CE marking cannot be considered a “safety mark” for consumers.

In addition, CE marking is a self-certification scheme. Retailers sometimes refer to products as “CE approved,” but the CE marking does not actually signify approval. As mentioned above, certain categories of products (such as Class IIa, Class IIb and Class III medical devices) require involvement of a Notified Body to ensure conformity with relevant technical standards, but CE marking by the manufacturer in itself does not certify that this has been done.

Our facilities manufacturing medical devices for the EEA market are EN ISO 13485 (Medical devices - Quality management systems - Requirements for regulatory purposes) Certified. Moreover, our Waterlase and Diode laser systems have a CE marking. In addition, we have attained the proper licensing for Waterlase and Diode laser systems for sale in Canada, meeting the Canadian Medical Device Regulation requirements as part of the ISO certification process.

Other U.S. Regulation

We and our subcontractors also must comply with numerous federal, state and local laws relating to matters such as safe working conditions, manufacturing practices, environmental protection, fire hazard control, and hazardous substance disposal. Furthermore, we are subject to various reporting requirements including those prescribed by the Affordable Care Act and the Dodd-Frank Wall Street Reform and Consumer Protection Act. We cannot be sure that we will not be required to incur significant costs to comply with these laws and regulations in the future or that these laws or regulations will not adversely affect our business, financial condition, and results of operations. Unanticipated changes in existing regulatory requirements or the adoption of new requirements could adversely affect our business, financial condition, and results of operations.

Environmental

Our manufacturing processes involve the use, generation, and disposal of hazardous materials and wastes, including alcohol, adhesives, and cleaning materials. As such, we are subject to stringent federal, state, and local laws relating to the protection of the environment, including those governing the use, handling, and disposal of hazardous materials and wastes. Future environmental laws may require us to alter our manufacturing processes, thereby increasing our manufacturing costs. We believe that our products and manufacturing processes at our facilities comply in all material respects with applicable environmental laws and worker health and safety laws. However, the risk of environmental liabilities cannot be completely eliminated.

Health Care Fraud and Abuse

As a medical device manufacturer, our operations and interactions with health care providers, including dentists, are subject to extensive laws and regulations imposed at the federal, state, and local level in the U.S., including, but not limited to, those discussed in this Form 10-K. In the U.S., there are federal and state anti-kickback statutes that generally prohibit the payment or receipt of kickbacks, bribes, or other remuneration in exchange for the referral of patients or other health-related business. For example, the federal Anti-Kickback Statute is a criminal statute that prohibits anyone from, among other things, knowingly and willfully offering, paying, soliciting, or receiving any bribe, kickback, or other remuneration intended to induce a referral for the furnishing of, or the purchase, order, or recommendation of, any item or service reimbursable under the Federal health care programs (“FHCPs”), including Medicare, Medicaid, and TRICARE. Recognizing that the federal Anti-Kickback Statute is broad and potentially applicable to many commonplace arrangements, the U.S. Congress and the Office of Inspector General (“OIG”) within the Department of Health and Human Services (“HHS”) have created statutory “exceptions” and regulatory “safe harbors” to the federal Anti-Kickback Statute. Exceptions and safe harbors exist for a number of arrangements relevant to our business, including, among other things, certain payments to bona fide employees, certain discount and rebate arrangements, and certain payment arrangements with health care providers, assuming all elements of the relevant exception/safe harbor have been satisfied. Although an arrangement that fits squarely into one or more of these exceptions or safe harbors generally will not be subject to prosecution, OIG has also cautioned in various contexts that even where each component of an arrangement has been structured to satisfy a safe harbor, the components, as part of an overall arrangement, may still violate the federal Anti-Kickback Statute. However, arrangements that do not fit squarely within an exception or safe harbor do not necessarily violate the federal Anti-Kickback Statute. Rather, OIG and/or other government enforcement authorities will examine the facts and circumstances relevant to the specific arrangement to determine whether it involves the sorts of abuses that the statute was designed to combat. Violations of this federal law constitute a felony offense punishable by imprisonment, criminal fines of up to \$25,000, civil fines of up to \$74,792 per violation (as adjusted for annual inflation) and three times the amount of the unlawful remuneration, and exclusion from Medicare, Medicaid, and other FHCPs. Exclusion of a manufacturer like us would preclude any FHCP from paying for the manufacturer’s products. In addition, pursuant to the changes made by the Affordable Care Act, a claim resulting from a violation of the federal Anti-Kickback Statute may serve as the basis for a false claim under the federal Civil False Claims Act. Many states also have their own laws that parallel and implicate anti-kickback restrictions, but may apply regardless of whether any FHCP business is involved. Federal and state anti-kickback laws may affect our sales, marketing and promotional activities, educational programs, pricing and discount practices and policies, and relationships with dental and medical providers by limiting the kinds of arrangements we may have with hospitals, alternate care market providers, physicians, dentists, and others in a position to purchase or recommend our products.

Federal and state false claims laws prohibit anyone from presenting, or causing to be presented, claims for payment to third-party payers that are false or fraudulent. For example, the federal Civil False Claims Act imposes liability on any person or entity that knowingly presents, or causes to be presented, a false or fraudulent claim for payment to the government, including FHCPs. Some suits filed under the Civil False Claims Act can be brought by a “whistleblower” or a “relator” on behalf of the government, and such individuals may share in any amounts paid by the entity to the government in fines or settlement. Manufacturers, like us, can be held liable under false claims laws, even if they do not submit claims to the government, where they are found to have caused submission of false claims by, among other things, providing incorrect coding or billing advice about their products to customers that file claims, or by engaging in kickback arrangements with customers that file claims. A violation of the Civil False Claims Act could result in fines of up to \$21,916 (as adjusted for annual inflation) for each false claim, plus up to three times the amount of damages sustained by the government. A Civil False Claims Act violation may also provide the basis for the imposition of administrative penalties and exclusion from participation in FHCPs. In addition to the Civil False Claims Act, the federal government also can use several criminal statutes to prosecute persons who are alleged to have submitted false or fraudulent claims for payment to the federal government, or improperly retained funds received which were not due. Moreover, a number of states also have false claims laws, and some of these laws may apply to claims for items or services reimbursed under Medicaid and/or commercial insurance.

In addition to the general fraud statutes mentioned above, there are a variety of other fraud and abuse laws specific to health care. For example, the Health Insurance Portability and Accountability Act of 1996 (“HIPAA”) created several new federal crimes, including health care fraud and false statements related to health care matters. The health care fraud statute prohibits, among other things, knowingly and willfully executing a scheme to defraud any health care benefit program, including private payers. A violation of this statute is a felony and may result in fines, up to ten years imprisonment (assuming no serious bodily injury or death results), or exclusion from FHCPS. The false statements statute prohibits, among other things, knowingly and willfully falsifying, concealing or covering up a material fact, or making any materially false, fictitious, or fraudulent statement in connection with the delivery of or payment for items or services under a health care benefit program. A violation of this statute is a felony and may result in fines and imprisonment and could potentially result in the government’s pursuit of exclusion from FHCPS. Additionally, a person who offers or transfers to a Medicare or Medicaid beneficiary any remuneration that the person knows or should know is likely to influence the beneficiary’s selection of a particular provider, practitioner, or supplier of items or services payable by Medicare or Medicaid may be liable for civil money penalties of up to \$10,000 for each item or service and potential exclusion from FHCPS.

The Physician Payments Sunshine Act requires us to report annually to the Centers for Medicare and Medicaid Services (“CMS”) certain payments and other transfers of value we make to U.S.-licensed physicians, dentists, and teaching hospitals. These annual reports are publicly available, which could impact the number of health care providers who are willing to work with us on the research and development of our products. In addition, several states have implemented similar transparency and disclosure laws applicable to medical device manufacturers, some of which require reporting of transfers of value made to a wider variety of health care professionals and institutions.

The federal physician self-referral prohibition (the “Stark Law”) is a strict liability statute, which, in the absence of a statutory or regulatory exception, prohibits: (i) the referral of Medicare and Medicaid patients by a physician to an entity for the provision of designated health care services if the physician or a member of the physician’s immediate family has a direct or indirect financial relationship, including an ownership interest in, or a compensation arrangement with, the entity and (ii) the submission of a bill to Medicare or Medicaid for services rendered pursuant to a prohibited referral. Penalties for violations of the Stark Law include denial of payment for the service, required refund of payments received pursuant to the prohibited referral, and civil monetary penalties for knowing violations of up to \$24,253 per claim (as adjusted for annual inflation), up to \$161,692 for circumvention schemes, and up to \$11,052 per day for failing to report information concerning the entity’s ownership, investment, and compensation arrangements upon HHS’ request. Stark Law violations also may lead to False Claims Act liability and possible exclusion from FHCPS.

The FCPA’s anti-bribery provisions generally prohibit companies and their intermediaries from offering to pay, promising to pay, or authorizing the payment of money or anything of value to non-U.S. officials for the purpose of influencing any act or decision of the foreign official in his/her capacity or to secure any other improper advantage to obtain or retain business. Violation of the anti-bribery provisions of the FCPA by a corporation or business entity can result in criminal fines of up to \$2 million and civil penalties of up to \$16,000 for each violation. Individuals, including officers, directors, stockholders, and agents of companies, can be subject to a criminal fine of up to \$250,000 and/or imprisonment, in addition to civil penalties of up to \$16,000, per violation.

The FCPA’s accounting provisions require that all issuers 1) make and keep books, records, and accounts that, in reasonable detail, accurately and fairly reflect an issuer’s transactions and dispositions of an issuer’s assets; and 2) devise and maintain a system of internal accounting controls sufficient to ensure management’s control, authority, and responsibility over the firm’s assets. Violations of the accounting provisions by a corporation or other business entity can result in criminal fines of up to \$25 million per violation and civil penalties of up to \$725,000. Individuals can be subject to a criminal fine of up to \$5 million per violation and/or imprisonment and civil penalties of up to \$150,000.

Due to the breadth of some of these laws, it is possible that some of our current or future practices might be challenged under one or more of these laws. In addition, there can be no assurance that we would not be required to alter one or more of our practices to comply with these laws. Evolving interpretations of current laws or the adoption of new federal or state laws or regulations could adversely affect some of the arrangements we have with customers, physicians, and dentists. If our past or present operations are found to be in violation of any of these laws, we could be subject to civil and criminal penalties, which could hurt our business, financial condition, and results of operations.

Privacy and Security of Health Information

Numerous federal, state, and international laws and regulations govern the collection, use, and disclosure of patient-identifiable health information, including HIPAA. HIPAA applies to covered entities, which include, among other entities, a “health care provider” that transmits health information in electronic form in connection with certain transactions regulated under HIPAA. HIPAA also applies to “business associates,” meaning persons or entities that create, receive, maintain, or transmit protected health information (“PHI”) to perform a function on behalf of, or provide a service to, a covered entity. Although we are not a covered entity, most health care (including dental) facilities that purchase our products are covered entities under HIPAA. Due to activities that we perform for or on behalf of covered entities, we may sometimes act as a business associate, or our customers may ask us to enter Business Associate Agreements and assume business associate responsibilities.

Various implementing regulations have been promulgated under HIPAA. The HIPAA Security Rule requires implementation of certain administrative, physical, and technical safeguards to ensure the confidentiality, integrity, and availability of electronic PHI. The HIPAA Privacy Rule governs the use and disclosure of PHI and provides certain rights to individuals with respect to that information. For example, for most uses and disclosures of PHI, other than for treatment, payment, health care operations, and certain public policy purposes, the HIPAA Privacy Rule generally requires obtaining valid written authorization from the individual, including in the research context. With certain limited exceptions, the covered entity performing the research must obtain valid authorization from the research subject (or an appropriate waiver) before providing that subject’s PHI to sponsors like us. Furthermore, in most cases, the HIPAA Privacy Rule requires that use or disclosure of PHI be limited to the minimum necessary to achieve the purpose of the use or disclosure.

The HIPAA Privacy and Security Rules require covered entities to contractually bind us, where we are acting as a business associate, to protect the privacy and security of individually identifiable health information that we may use, access, or disclose for purposes of services we may provide. Moreover, the Health Information Technology for Economic and Clinical Health Act (“HITECH”) enacted in February 2009, made certain provisions of the HIPAA Privacy and Security Rules directly applicable to business associates.

HITECH also established new breach notification requirements, increased civil penalty amounts for HIPAA violations, and requires HHS to conduct periodic audits of covered entities and business associates to confirm compliance. In addition, HITECH authorizes state attorneys general to bring civil actions in response to HIPAA violations committed against residents of their respective states.

In 2013, the Office for Civil Rights (“OCR”) of HHS released an omnibus final rule (the “Final Rule”), implementing HITECH. Among other provisions, the Final Rule made certain changes to the breach notification regulations, including requiring business associates to notify covered entities if a breach occurs at or by the business associate. Following a breach of unsecured PHI, covered entities must provide notification of the breach to affected individuals, the HHS Secretary, and, for breaches affecting more than 500 residents of a state or jurisdiction, prominent media outlets serving that state/jurisdiction. Breaches of health information can also give rise to class actions by affected individuals and result in significant reputational damage to the covered entity and/or business associates or other parties involved in the breach.

The Final Rule also provides for heightened governmental investigations of potential non-compliance. However, the Final Rule did not address accounting of disclosures, although such regulations are forthcoming. The proposed rule addressing accounting of disclosures, if finalized, could impose a significant burden on us, as it would require covered entities and their business associates to develop systems to monitor (1) which employees access an individual's electronic PHI contained in a designated record set, (2) the time and date such access occurs, and (3) the action taken during the access session (e.g., modification, deletion, viewing).

Failure to comply with HIPAA may result in civil and criminal penalties. Civil penalties for a single violation of the regulations occurring on or after February 18, 2009 range from \$110 to more than \$55,000 per violation, with a maximum penalty of \$1,650,300 per year for violations of an identical provision of the regulations. Criminal penalties of up to \$250,000 and imprisonment may also be imposed for certain knowing violations of HIPAA. We may be required to make costly system modifications, which may restrict our business operations, to comply with HIPAA, to the extent we act as a business associate. Our failure to comply may result in liability and adversely affect our business, financial condition, and results of operations.

Numerous other federal and state laws protect the confidentiality of patient information, including state medical privacy laws and federal and state consumer protection laws. These state laws may be similar to or possibly more stringent than the federal provisions. These laws in many cases are not preempted by the HIPAA rules and may be subject to varying interpretations by the courts and government agencies, creating complex compliance issues for us and our customers and potentially exposing us to additional expense, adverse publicity, and liability. Other countries also have, or are developing, laws governing the collection, use, and transmission of personal or patient information, which could create liability for us or increase our cost of doing business.

New health information standards, whether implemented pursuant to HIPAA, future Congressional action, or otherwise, could have a significant effect on the manner in which we handle health information, and the cost of complying with these standards could be significant. If we do not properly comply with existing or new laws and regulations related to patient health information, we could be subject to criminal or civil sanctions.

Third-Party Reimbursement

Dentists and other health care providers that purchase our products may rely on third-party payers, including Medicare, Medicaid, and private payers to cover and reimburse all or part of the cost of the clinical procedures performed using our products. As a result, demand for our products is dependent in part on the coverage and reimbursement policies of these payers. We believe that most of the procedures being performed with our current products generally are reimbursable, with the exception of cosmetic applications, such as teeth whitening.

No uniform coverage or reimbursement policy for dental and medical treatment exists among third-party payers, and coverage and reimbursement can differ significantly from payer to payer. Under Medicaid, for example, states are required to cover basic dental services for children, but retain discretion as to whether to provide coverage for dental services for adults. Under the Early Periodic Screening, Diagnostic, and Treatment benefit available to children, dental services determined to be “medically necessary” and provided at intervals that meet reasonable standards of dental practice (or at such other intervals, as indicated by medical necessity) are generally covered by Medicaid. Although not required to cover dental services for adults, most state Medicaid programs still provide a degree of coverage for at least emergency dental services.

Medicare covers dental services only in certain limited circumstances. For instance, Medicare will pay for certain dental services when provided in the inpatient hospital setting if the dental procedure itself made hospitalization necessary. Medicare will also pay for certain dental services that are an integral part of a covered procedure (e.g., jaw reconstruction following accidental injury), extractions done in preparation for certain radiation treatments, and oral examinations preceding kidney transplantation or heart valve replacement, under certain circumstances.

Future legislation, regulation or coverage and reimbursement policies of third-party payers may adversely affect the demand for our products. For example, the Affordable Care Act included various reforms impacting Medicare reimbursement and coverage, including revision to prospective payment systems, any of which may adversely impact any Medicare reimbursements received by our end-user customers. Moreover, the Budget Control Act of 2011, enacted on August 2, 2011, established a process to reduce federal budget deficits through an automatic “sequestration” process if deficit reductions targets are not otherwise reached. Under the terms of the Budget Control Act, sequestration imposes cuts to a wide range of federal programs, including Medicare, which is subject to a 2% cut. The Bipartisan Budget Act of 2015 extended the 2% sequestration cut for Medicare through fiscal year 2025 and realigned the fiscal year 2025 Medicare sequestration amounts so that there will be a 4% sequester for the first six months and a 0% sequester for the second six months, instead of a 2% sequester for the full 12-month period.

In addition, private payers and employer-sponsored health care plans became subject to various rules and potential penalties under the Affordable Care Act. For example, health plans in the individual and small group markets were required to begin providing a core package of health care services, known as “essential health benefits.” Essential health benefits include ten general categories of care, including pediatric services, which requires coverage of dental and vision care, among other medical services, for children. The Affordable Care Act also required employers with 50 or more employees to offer health insurance coverage to full-time workers or pay a penalty, which could potentially increase the availability of third-party reimbursement for some medical procedures using our products, although we continue to assess the impact of the Affordable Care Act on our business.

We cannot be sure that government or private third-party payers will cover and reimburse the procedures using our products in whole or in part in the future or that payment rates will be adequate.

Because third-party payments may be less than a provider’s actual costs in furnishing care, providers have incentives to lower their operating costs by utilizing products that will decrease labor or otherwise lower their costs. However, we cannot be certain that dental and medical service providers will purchase our products, despite the clinical benefits and opportunity for cost savings that we believe can be derived from their use. If providers cannot obtain adequate coverage and reimbursement for our products, or the procedures in which they are used, our business, financial condition, and results of operations could suffer.

Employees

At December 31, 2017, the Company employed approximately 195 people. Our employees are not represented by any collective bargaining agreement, and we believe our employee relations are good.

Executive Officers of the Registrant

The executive officers of the Company are elected each year at the meeting of our Board, which follows the annual meeting of stockholders, and at other Board meetings, as appropriate.

At March 14, 2018, the executive officers of the Company were as follows:

Name	Age	Position
Harold C. Flynn, Jr.	52	President and Chief Executive Officer
John R. Beaver	56	Senior Vice President and Chief Financial Officer
Dmitri Boutoussov, Ph.D.	54	Vice President of Research and Development
Ryan T. Meardon	38	Vice President of U.S. Sales
Richard R. Whipp	65	Vice President of Operations

Harold C. Flynn was named President and Chief Executive Officer of BIOLASE in July 2015. Prior to joining BIOLASE, Mr. Flynn was the President of Zimmer Dental, a division of Zimmer Holdings Inc. and a leading manufacturer and provider of medical devices for the dental market, including implants, prosthetics, and a range of other oral rehabilitation products, from 2007 to 2015. From 2004 to 2007, Mr. Flynn was Divisional Vice President and General Manager at Abbott Hematology, a division of Abbott Laboratories. Prior to joining Abbott Hematology, Mr. Flynn spent 14 years in a variety of positions of increasing responsibility at IDEXX Laboratories, a global leader in veterinary, food, and environmental diagnostics. Mr. Flynn has a Bachelor of Science degree in Electrical Engineering from the University of Maine at Orono. He holds patents in laser-based hematology and implantable devices for dentistry.

John R. Beaver was named Senior Vice President and Chief Financial Officer in October 2017. Prior to joining BIOLASE, Mr. Beaver served as the Chief Financial Officer of Silicor Materials, Inc., a global leader in the production of solar silicon, from 2009 to 2013 and 2015 to 2017. Mr. Beaver also served on the Board of Directors of Silicor Materials, Inc. from 2013 to 2015. From 2013 to 2015, Mr. Beaver was Chief Financial Officer for Modumetal, Inc., a nano-laminated alloy coatings company focused on oil and gas applications. Prior to 2009, Mr. Beaver was Senior Vice President – Finance and Chief Financial Officer at Sterling Chemicals, a mid-sized public commodity chemical manufacturer. Mr. Beaver holds a Bachelor of Business Administration in Accounting from the University of Texas at Austin and is a Certified Public Accountant.

Dmitri Boutoussov, Ph.D. joined BIOLASE in 2000 as the Director of Engineering and advanced to Vice President of Engineering in 2005, Chief Technology Officer in 2010, and his current role as Vice President of Research and Development in July 2013. Mr. Boutoussov holds a Doctorate degree in Philosophy and a Master of Science degree in Physics from Polytechnic University in St. Petersburg, Russia.

Ryan T. Meardon joined BIOLASE in August 2011 as an Account Manager and advanced to the role of Sales Director in August 2013. In January 2018, Mr. Meardon was named Vice President of U.S. Sales. Prior to joining BIOLASE, Mr. Meardon served as a Regional Product Specialist and Key Account Manager for Brasseler USA, a dental and surgical instrumentation company, from 2005 to 2011. Mr. Meardon holds Bachelor of Arts and Masters of Science degrees in Kinesiology from The University of Colorado.

Richard R. Whipp joined BIOLASE in July 2011 as Director of Operations and was promoted to Vice President of Operations in October 2011. Prior to joining BIOLASE, Mr. Whipp served as Senior Director of Operations at Discus Dental, which became a division of Philips Electronics, from 1998 to 2011. From 1992 to 1998, Mr. Whipp was Director of Operations at Leica Geosystems, Inc. Mr. Whipp previously held operations management positions at Gulton Industries, Inc., Conrac Industries, Inc., and HydriL. Mr. Whipp holds a Bachelor of Science degree in Industrial Engineering from the Newark College of Engineering.

Available Information

Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to reports filed or furnished pursuant to Sections 13(a) and 15(d) of the Exchange Act, are available free of charge on our website at <http://www.biolase.com>, as soon as reasonably practicable after the Company electronically files such reports with, or furnishes those reports to, the SEC. We are providing our internet site solely for the information of investors. We do not intend the address to be an active link or to otherwise incorporate the contents of the website into this report.

Additional Information

BIOLASE®, ZipTip®, ezlase®, eztips®, ComfortPulse®, Waterlase®, Waterlase Dentistry®, Waterlase Express®, iLase®, iPlus®, Epic®, Epic Pro®, WCLI®, World Clinical Laser Institute®, Waterlase MD®, Waterlase Dentistry®, and EZLase® are registered

trademarks of BIOLASE, and Pedolase™ is a trademark of BIOLASE. All other product and company names are registered trademarks or trademarks of their respective owners.

Item 1A. Risk Factors

Investing in our securities involves a high degree of risk. You should carefully consider the following risk factors together with all of the other information included in this Form 10-K. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we presently consider to be immaterial could also adversely affect us. If any of the following risks come to fruition, our business, financial condition, results of operations, cash flows, and future growth prospects could be materially and adversely affected. In these circumstances, the market price of our stock could decline, and you could lose all or part of your investment.

Risks Related to Our Business and Operations

Although our financial statements have been prepared on a going concern basis, our management and independent auditors in their report accompanying our consolidated financial statements for the year ended December 31, 2017, believe that our recurring losses from operations and other factors have raised substantial doubt about our ability to continue as a going concern as of December 31, 2017.

Our audited financial statements for the fiscal year ended December 31, 2017 were prepared on a going concern basis in accordance with U.S. GAAP. The going concern basis assumes that we will continue in operation for the next 12 months and will be able to realize our assets and discharge our liabilities and commitments in the normal course of business. Thus, our financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern. Our recurring losses, negative cash flow, potential need for additional capital and the uncertainties surrounding our ability to raise such funding, raise substantial doubt about our ability to continue as a going concern. In order for us to continue operations beyond the next 12 months and be able to discharge our liabilities and commitments in the normal course of business, we must sell our products directly to end-users and through distributors, establish profitable operations through increased sales, decrease expenses, generate cash from operations or raise additional funds when needed. We intend to improve our financial condition and ultimately improve our financial results by increasing revenues through expansion of our product offerings, continuing to expand and develop our field sales force and distributor relationships both domestically and internationally, forming strategic arrangements within the dental and medical industries, educating dental and medical patients as to the benefits of our advanced medical technologies, and reducing expenses. If we are unable to increase sales, reduce expenses or raise sufficient additional capital we may be unable to continue to fund our operations, develop our products, realize value from our assets, or discharge our liabilities in the normal course of business. If we become unable to continue as a going concern, we could have to liquidate our assets, and potentially realize significantly less than the values at which they are carried on our financial statements, and stockholders could lose all or part of their investment in our common stock.

We have experienced net losses for each of the past three years and we could experience additional losses and have difficulty achieving profitability in the future.

We had an accumulated deficit of approximately \$195.6 million at December 31, 2017. We recorded net losses of approximately \$16.9 million, \$15.4 million, and \$20.3 million for the years ended December 31, 2017, 2016, and 2015, respectively. In order to achieve profitability, we must increase net revenue through new sales and control our costs. Failure to increase our net revenue and decrease our costs could cause our stock price to decline and could have a material adverse effect on our business, financial condition, and results of operations.

We are vulnerable to continued global economic uncertainty and volatility in financial markets.

Our business is highly sensitive to changes in general economic conditions as a seller of capital equipment to end users in dental professional practices. Financial markets inside the United States and internationally have experienced extreme disruption in recent times, including, among other things, extreme volatility in security prices, severely diminished liquidity and credit availability, and declining valuations of investments. We believe these disruptions are likely to have an ongoing adverse effect on the world economy. A continuing economic downturn and financial market disruptions could have a material adverse effect on our business, financial condition, and results of operations, including by:

- reducing demand for our products and services, increasing order cancellations and resulting in longer sales cycles and slower adoption of new technologies;
- increasing the difficulty of collecting accounts receivable and the risk of excess and obsolete inventories;

- increasing price competition in our served markets; and
- resulting in supply interruptions, which could disrupt our ability to produce our products.

We could need to raise additional capital in the future, and if we are unable to secure adequate funds on terms acceptable to us, we could be unable to execute our business plan.

To remain competitive, we must continue to make significant investments in the development of our products, the expansion of our sales and marketing activities, and the expansion of our operating and management infrastructure as we increase sales domestically and internationally. If cash generated from our operations is insufficient to fund such growth, we could be required to raise additional funds through the issuance of equity or debt securities in the public or private markets, or through a collaborative arrangement or sale of assets. Additional financing opportunities may not be available to us, or if available, may not be on favorable terms. The availability of financing opportunities will depend, in part, on market conditions, and the outlook for our business. Any future issuance of equity securities or securities convertible into equity securities could result in substantial dilution to our stockholders, and the securities issued in such a financing could have rights, preferences or privileges senior to those of our common stock. In addition, if we raise additional funds through debt financing, we could be subject to debt covenants that place limitations on our operations. We could not be able to raise additional capital on reasonable terms, or at all, or we could use capital more rapidly than anticipated. If we cannot raise the required capital when needed, we may not be able to satisfy the demands of existing and prospective customers, we could lose revenue and market share and we may have to curtail our capital expenditures. The following factors, among others, could affect our ability to obtain additional financing on favorable terms, or at all:

- our results of operations;
- general economic conditions and conditions in the dental or medical device industries;
- the perception of our business in the capital markets;
- our ratio of debt to equity;
- our financial condition;
- our business prospects; and
- interest rates.

If we are unable to obtain sufficient capital in the future, we could have to curtail our capital expenditures. Any curtailment of our capital expenditures could result in a reduction in net revenue, reduced quality of our products, increased manufacturing costs for our products, harm to our reputation, or reduced manufacturing efficiencies and could have a material adverse effect on our business, financial condition, and results of operations.

Our success depends, in part, on our relationships with, and the efforts of, third-party distributors.

We rely on exclusive and non-exclusive third-party distributors for a portion of our sales in North America and a majority of our sales in countries outside of the U.S. and Canada. For the fiscal years ended December 31, 2017, 2016, and 2015, revenue from distributors accounted for approximately 32%, 30%, and 34% of our total net revenue, respectively. Our distributors have significant discretion in determining the efforts and resources they apply to the sale of our products, and we face significant challenges and risks in expanding, training, and managing our third-party distributors, particularly given their geographically dispersed operations. Our distributors may not commit the necessary resources to market and sell our products to the level of our expectations, and, regardless of the resources they commit, they may not be successful. From time to time, we may face competition or pricing pressure from one or more of our non-exclusive distributors in certain geographic areas where those distributors are selling inventory to the same customer base as us. Additionally, most of our distributor agreements can be terminated with limited notice, and we may not be able to replace any terminating distributor in a timely manner or on terms agreeable to us, if at all. If we are not able to maintain our distribution network, if our distribution network is not successful in marketing and selling our products, or if we experience a significant reduction in, cancellation, or change in the size and timing of orders from our distributors, our revenues could decline significantly and could have a material adverse effect on our business, financial condition, and results of operations.

Dentists and patients have been hesitant in adopting laser technologies, and our inability to overcome this hesitation could limit the market acceptance of our products and our market share.

Our dental laser systems represent relatively new technologies in the dental market. Only a small percentage of dentists use lasers to perform dental procedures. Our future success will depend on our ability to increase demand for our products by demonstrating to a broad spectrum of dentists and patients the potential performance advantages of our laser systems over traditional methods of treatment and over competitive laser systems, and our inability to do so could have a material adverse effect on our business, financial condition, and results of operations. Historically, we have experienced long sales cycles because dentists have been, and could continue to be, slow to adopt new technologies on a widespread basis. As a result, we generally are required to invest a significant amount of time and resources to educate dentists about the benefits of our products in comparison to competing products and technologies before completing a sale, if any.

Factors that could inhibit adoption of laser technologies by dentists include cost and concerns about the safety, efficacy, and reliability of lasers. In order to invest in a Waterlase system, a dentist generally needs to invest time to understand the technology, consider how patients may respond to the new technology, assess the financial impact the investment could have on the dentist's practice and become comfortable performing procedures with our products. Absent an immediate competitive motivation, a dentist may not feel compelled to invest the time required to learn about the potential benefits of using a laser system. Dentists may not accept or adopt our products until they see additional clinical evidence supporting the safety and efficiency of our products or recommendations supporting our laser systems by influential dental practitioners. In addition, economic pressure, caused, for example, by an economic slowdown, changes in health care reimbursement or by competitive factors in a specific market, could make dentists reluctant to purchase substantial capital equipment or invest in new technologies. Patient acceptance will depend on the recommendations of dentists and specialists, as well as other factors, including the relative effectiveness, safety, reliability, and comfort of our systems as compared to other instruments and methods for performing dental procedures.

Any failure in our efforts to train dental practitioners could result in the misuse of our products, reduce the market acceptance of our products and have a material adverse effect on our business, financial condition, and results of operations.

There is a learning process involved for dental practitioners to become proficient users of our laser systems. It is critical to the success of our sales efforts to adequately train a sufficient number of dental practitioners. Following completion of training, we rely on the trained dental practitioners to advocate the benefits of our products in the broader marketplace. Convincing dental practitioners to dedicate the time and energy necessary for adequate training is challenging, and we cannot provide assurance that we will be successful in these efforts. If dental practitioners are not properly trained, they could misuse or ineffectively use our products, or could be less likely to appreciate our laser systems. This could also result in unsatisfactory patient outcomes, patient injury, negative publicity, FDA regulatory action, or lawsuits against us, any of which could negatively affect our reputation and sales of our laser systems.

If future data proves to be inconsistent with our clinical results or if competitors' products present more favorable results our revenues could decline and our business, financial condition, and results of operations could be materially and adversely affected.

If new studies or comparative studies generate results that are not as favorable as our clinical results, our revenues could decline. Additionally, if future studies indicate that our competitors' products are more effective or safer than ours, our revenues could decline. Furthermore, dental practitioners could choose not to purchase our laser systems until they receive additional published long-term clinical evidence and recommendations from prominent dental practitioners that indicate our laser systems are effective for dental applications.

We face competition from other companies, many of which have substantially greater resources than we do. If we do not successfully develop and commercialize enhanced or new products that remain competitive with products or alternative technologies developed by others, we could lose revenue opportunities and customers and our ability to grow our business would be impaired.

A number of competitors have substantially greater capital resources, larger customer bases, larger technical, sales and marketing forces and stronger reputations with target customers than ours. We compete with a number of domestic and foreign companies that market traditional dental products, such as dental drills, as well as companies that market laser technologies in the dental and medical markets. The marketplace is highly fragmented and very competitive. We expect that the rapid technological changes occurring in the health care industry could lead to the entry of new competitors, particularly if dental and medical lasers gain increasing market acceptance. If we do not compete successfully, our revenue and market share could decline and our business, financial condition, and results of operations could be adversely affected.

Our long-term success depends upon our ability to (i) distinguish our products through improving our product performance and pricing, protecting our intellectual property, improving our customer support, accurately timing the introduction of new products, and developing sustainable distribution channels worldwide; and (ii) develop and successfully commercialize new products, new or improved technologies, and additional applications for our laser systems. There is no assurance that we will be able to distinguish our products and commercialize any new products, new or improved technologies, or additional applications for our laser systems.

If our customers cannot obtain third-party reimbursement for their use of our products, they could be less inclined to purchase our products and our business, financial condition, and results of operations could be adversely affected.

Our products are generally purchased by dental or medical professionals who have various billing practices and patient mixes. Such practices range from primarily private pay to those who rely heavily on third-party payers, such as private insurance or government programs. In the United States, third-party payers review and frequently challenge the prices charged for medical products and/or services. In many foreign countries, the prices for dental services are predetermined through government regulation. Payers could deny coverage and reimbursement on various grounds, including if they determine that the procedure was not medically necessary or that the device used in the procedure was investigational. Accordingly, both coverage and reimbursement can vary significantly from payer to payer. For the portion of dentists who rely heavily on third-party reimbursement, the inability to obtain reimbursement for services using our products could deter them from purchasing or using our products. We cannot predict the effect that future health care reforms or changes in financing for health and dental plans could have on our business. Any such changes could have an adverse effect on the ability of a dental or medical professional to generate a profit using our current or future products. In addition, such changes could act as disincentives for capital investments by dental and medical professionals.

Our ability to use net operating loss carryforwards could be limited.

Section 382 of the Internal Revenue Code of 1986 (“IRC”) generally imposes an annual limitation on the amount of net operating loss carryforwards that may be used to offset taxable income when a corporation has undergone material changes in its stock ownership. In 2006, we completed an analysis to determine the applicability of the annual limitations imposed by IRC Section 382 caused by previous changes in our stock ownership and determined that such limitations should not be significant. Given our continued generation of losses since the completion of 2006 study, we have not updated the study. However, we plan to update the study if we expect to utilize net operating loss carryforwards in any future year. If we experience an ownership change as defined in IRC Section 382, utilization of the net operating loss carryforwards, research and development credit carryforwards, and other tax attributes, would be subject to an annual limitation under Section 382 of the IRC. In addition, our ability to utilize net operating loss carryforwards, research and development credit carryforwards, and other tax attributes may be limited by other changes outside our control, such as changes to applicable tax law. Any limitation may result in the expiration of a portion of the net operating loss or research and development credit carryforwards before utilization. If we lose our ability to use net operating loss carryforwards, any income we generate will be subject to tax earlier than it would be if we were able to use net operating loss carryforwards, resulting in lower profits which could have a material adverse effect on our business, financial condition, and results of operations.

We could incur problems in manufacturing our products.

In order to grow our business, we must expand our manufacturing capabilities to produce the systems and accessories necessary to meet any demand we may experience. We could encounter difficulties in increasing the production of our products, including problems involving production capacity and yields, quality control and assurance, component supply, and shortages of qualified personnel. In addition, before we can begin commercial manufacture of our products, we must ensure our manufacturing facilities, processes, and quality systems, and the manufacture of our laser systems, comply with FDA regulations governing facility compliance, quality control, and documentation policies and procedures. In addition, our manufacturing facilities are subject to periodic inspections by the FDA, as well as various state agencies and foreign regulatory agencies. From time to time, we could expend significant resources in obtaining, maintaining, and addressing our compliance with these requirements. Our success will depend in part upon our ability to manufacture our products in compliance with the FDA’s QSR and other regulatory requirements. We have experienced quality issues with components of our products supplied by third parties, and we could continue to do so. Our future success depends on our ability to manufacture our products on a timely basis with acceptable manufacturing costs, while at the same time maintaining good quality control and complying with applicable regulatory requirements, and an inability to do so could have a material adverse effect on our business, financial condition, and results of operations

We could be subject to significant warranty obligations if our products are defective, which could have a material adverse effect on our business, financial condition, and results of operations.

In manufacturing our products, we depend upon third parties for the supply of various components. Many of these components require a significant degree of technical expertise to design and produce. If we fail to adequately design, or if our suppliers fail to produce components to specification, or if the suppliers, or we, use defective materials or workmanship in the manufacturing process, the reliability and performance of our products will be compromised. We have experienced such non-compliance with manufacturing specifications in the past and could continue to experience such non-compliance in the future, which could lead to higher costs and reduced margins.

Our products could contain defects that cannot be repaired easily and inexpensively, and we have experienced in the past and could experience in the future some or all of the following:

- loss of customer orders and delay in order fulfillment;
- damage to our brand reputation;
- increased cost of our warranty program due to product repair or replacement;
- inability to attract new customers;
- diversion of resources from our manufacturing and engineering and development departments into our service department; and
- legal action.

Adverse publicity regarding our technology or products could negatively impact us.

Adverse publicity regarding any of our products or similar products marketed or sold by others could negatively affect us. If any studies raise or substantiate concerns regarding the efficacy or safety of our products or other concerns, our reputation could be harmed and demand for our products could diminish, which could have a material adverse effect on our business, financial condition, and results of operations.

Our products are used in minimally invasive surgical procedures, usually, though not always, without anesthesia. All surgical procedures carry some risk. Patients could experience adverse events or outcomes following a surgical procedure due to a multitude of different factors alone or in combination, including deficits in the skill, experience, and preparedness of the surgeon, the existence of underlying conditions or overall poor health of the patient, and defects, age, and misuse of medical products used in the procedure. Should an adverse patient event occur during the use of a BIOLASE product, there could be adverse publicity, increased scrutiny from regulatory agencies, and a loss of good will, even if it is ultimately shown to be caused by factors other than a BIOLASE product.

Product liability claims against us could be costly and could harm our reputation.

The sale of dental and medical devices involves the risk of product liability claims against us. Claims could exceed our product liability insurance coverage limits. Our insurance policies are subject to various standard coverage exclusions, including damage to the product itself, losses from recall of our product, and losses covered by other forms of insurance such as workers compensation. We cannot be certain that we will be able to successfully defend any claims against us, nor can we be certain that our insurance will cover all liabilities resulting from such claims. In addition, we cannot provide assurance that we will be able to obtain such insurance in the future on terms acceptable to us, or at all. Regardless of merit or eventual outcome, any product liability claim brought against us could result in harm to our reputation, decreased demand for our products, costs related to litigation, product recalls, loss of revenue, an increase in our product liability insurance rates, or the inability to secure coverage in the future, and could have a material adverse effect on our business, financial condition, and results of operations.

Our suppliers may not supply us with a sufficient amount or adequate quality of materials, which could have a material adverse effect on our business, financial condition, and results of operations.

Our business depends on our ability to obtain timely deliveries of materials, components, and subassemblies of acceptable quality and in acceptable quantities from third-party suppliers. We generally purchase components and subassemblies from a limited group of suppliers through purchase orders, rather than written supply contracts. Consequently, many of our suppliers have no obligation to continue to supply us on a long-term basis. In addition, our suppliers manufacture products for a range of customers, and fluctuations in demand for the products those suppliers manufacture for others could affect their ability to deliver components for us in a timely manner. Moreover, our suppliers could encounter financial hardships, be acquired, or experience other business events unrelated to our demand for components, which could inhibit or prevent their ability to fulfill our orders and satisfy our requirements.

Certain components of our products, particularly specialized components used in our laser systems, are currently available only from a single source or limited sources. For example, the crystal, fiber, and hand pieces used in our Waterlase systems are each supplied by a separate single supplier. Our dependence on single-source suppliers involves several risks, including limited control over pricing, availability, quality, and delivery schedules.

If any of our suppliers cease to provide us with sufficient quantities of our components in a timely manner or on terms acceptable to us, or ceases to manufacture components of acceptable quality, we could incur manufacturing delays and sales disruptions while we locate and engage alternative qualified suppliers, and we might be unable to engage acceptable alternative suppliers on favorable terms. In addition, we could need to reengineer our components, which could require product redesign and submission to the FDA of a 510(k) application, which could significantly delay production. Any interruption or delay in the supply of components or materials, or our inability to obtain components or materials from alternate sources at acceptable prices in a timely manner, could impair our ability to meet the demand of our customers and cause them to cancel orders or switch to competitive procedures. As of the date on which this Form 10-K was filed with the SEC, we were in the process of identifying and qualifying alternate source suppliers for our key components. There can be no assurance, however, that we will successfully identify and qualify an alternate source supplier for any of our key components or that we could enter into an agreement with any such alternate source supplier on terms acceptable to us, or at all.

Rapidly changing standards and competing technologies could harm demand for our products, result in significant additional costs, and have a material adverse effect on our business, financial condition, and results of operations.

The markets in which our products compete are subject to rapid technological change, evolving industry standards, changes in the regulatory environment, and frequent introductions of new devices and evolving dental and surgical techniques. Competing products could emerge that render our products uncompetitive or obsolete. The process of developing new medical devices is inherently complex and requires regulatory approvals or clearances that can be expensive, time-consuming, and uncertain. We cannot guarantee that we will successfully identify new product opportunities, identify new and innovative applications of our technology, or be financially or otherwise capable of completing the research and development required to bring new products to market in a timely manner. An inability to expand our product offerings or the application of our technology could limit our growth. In addition, we could incur higher manufacturing costs if manufacturing processes or standards change, and we could need to replace, modify, design, or build and install equipment, all of which would require additional capital expenditures.

We could be unable to effectively manage and implement our growth strategies, which could have a material adverse effect on our business, financial condition, and results of operations.

Our growth strategy includes expanding our product line and clinical applications by developing enhancements and transformational innovations, including new clinical solutions for dental applications and for other adjacent medical applications. Expansion of our existing product line and entry into new medical applications divert the use of our resources and systems, require additional resources that might not be available (or available on acceptable terms), require additional country-specific regulatory approvals, result in new or increasing competition, could require longer implementation times or greater start-up expenditures than anticipated, and could otherwise fail to achieve the desired results in a timely fashion, if at all. These efforts could also require that we successfully commercialize new technologies in a timely manner, price them competitively and cost-effectively, and manufacture and deliver sufficient volumes of new products of appropriate quality on time. We could be unable to increase our sales and earnings by expanding our product offerings in a cost-effective manner, and we could fail to accurately predict future customer needs and preferences or to produce viable technologies. In addition, we could invest heavily in research and development of products that do not lead to significant revenue. Even if we successfully innovate and develop new products and product enhancements, we could incur substantial costs in doing so. In addition, promising new products could fail to reach the market or realize only limited commercial success because of efficacy or safety concerns, failure to achieve positive clinical outcomes, or uncertainty over third-party reimbursement.

We have significant international sales and are subject to risks associated with operating in international markets.

International sales comprise a significant portion of our net revenue, and we intend to continue to pursue and expand our international business activities. For the fiscal years ended December 31, 2017, 2016, and 2015, international sales accounted for approximately 38%, 36%, and 39% of our net revenue, respectively. Political and economic conditions outside the United States could make it difficult for us to increase our international revenue or to operate abroad. International operations are subject to many inherent risks, which could have a material adverse effect on our business, financial condition, and results of operations, including among others:

- adverse changes in tariffs and trade restrictions;
- political, social, and economic instability and increased security concerns;
- fluctuations in foreign currency exchange rates;

- longer collection periods and difficulties in collecting receivables from foreign entities;
- exposure to different legal standards;
- transportation delays and difficulties of managing international distribution channels;
- reduced protection for our intellectual property in some countries;
- difficulties in obtaining domestic and foreign export, import, and other governmental approvals, permits, and licenses, and compliance with foreign laws;
- the imposition of governmental controls;
- unexpected changes in regulatory or certification requirements;
- difficulties in staffing and managing foreign operations; and
- potentially adverse tax consequences and the complexities of foreign value-added tax systems.

We believe that international sales will continue to represent a significant portion of our net revenue, and we intend to expand our international operations further. In international markets where our sales are denominated in U.S. dollars, an increase in the relative value of the dollar against the currency in such markets could indirectly increase the price of our products in those markets and result in a decrease in sales. We do not currently engage in any transactions as a hedge against risks of loss due to foreign currency fluctuations. However, we could do so in the future.

We could be subject to breaches of our information technology systems, which could damage our reputation and customer relationships. Such breaches could subject us to significant reputational, financial, legal, and operational consequences.

We rely on information systems (“IS”) in our business to obtain, rapidly process, analyze and manage data to, among other things:

- facilitate the purchase and distribution of thousands of inventory items through numerous distributors;
- receive, process and ship orders on a timely basis;
- accurately bill and collect from thousands of customers;
- process payments to suppliers; and
- provide technical support to our customers.

A cyber-attack that bypasses our IS security, or employee error, malfeasance or other disruptions that cause an IS security breach could lead to a material disruption of our IS and/or the loss of business information. Such an attack could result in, among other things:

- the theft, destruction, loss, misappropriation or release of confidential data and intellectual property;
- operational or business delays;
- liability for a breach of personal financial and health information belonging to our customers and their patients or to our employees; and
- damage to our reputation

any of which could have a material adverse effect on our business, financial condition, and results of operations. In the event of an attack, we would be exposed to a risk of loss or litigation and possible liability, including under laws that protect the privacy of personal information.

Our revenue and operating results fluctuate due to seasonality and other factors, so you should not rely on quarter-to-quarter comparisons of our operating results as an indication of our future performance.

Our revenue typically fluctuates from quarter to quarter due to a number of factors, many of which are beyond our control. Revenue in the first quarter typically is lower than average, and revenue in the fourth quarter typically is stronger than average due to the buying patterns of dental practitioners. We believe that this trend exists because a significant number of dentists purchase their capital equipment towards the end of the calendar year in order to maximize their practice earnings while seeking to minimize their taxes. They often use certain tax incentives, such as accelerated depreciation methods for purchasing capital equipment, as part of their year-end tax planning. In addition, revenue in the third quarter could be affected by vacation patterns, which can cause revenue to be flat or lower than in the second quarter of the year. Our historical seasonal fluctuations could also be impacted by sales promotions used by large dental distributors that encourage end-of-quarter and end-of-year buying in our industry. Other factors that might cause quarterly fluctuations in our revenue and operating results include the following:

- variation in demand for our products;
- our ability to research, develop, market, and sell new products and product enhancements in a timely manner;
- our ability to control costs;
- our ability to control quality issues with our products;
- regulatory actions that impact our manufacturing processes;
- the size, timing, rescheduling, or cancellation of orders from distributors;
- the introduction of new products by competitors;
- the length of and fluctuations in sales cycles;
- the availability and reliability of components used to manufacture our products;
- changes in our pricing policies or those of our suppliers and competitors, as well as increased price competition in general;
- legal expenses, particularly related to litigation matters;
- general economic conditions including the availability of credit for our existing and potential customer base to finance purchases;
- the mix of our domestic and international sales and the risks and uncertainties associated with international business;
- costs associated with any future acquisitions of technologies and businesses;
- limitations on our ability to use net operating loss carryforwards under the provisions of IRC Section 382 and similar state laws;
- developments concerning the protection of our intellectual property rights;
- catastrophic events such as hurricanes, floods, and earthquakes, which can affect our ability to advertise, sell, and distribute our products, including through national conferences held in regions in which these disasters strike; and
- global economic, political, and social events, including international conflicts and acts of terrorism.

The expenses we incur are based, in large part, on our expectations regarding future net revenue. Since many of our costs are fixed in the short term, we could be unable to reduce expenses quickly enough to avoid losses if we experience a decrease in expected net revenue. Accordingly, you should not rely on quarter-to-quarter comparisons of our operating results as an indication of our future performance.

Litigation against us could be costly and time-consuming to defend and could materially and adversely affect our business, financial condition, and results of operations.

We are from time to time involved in various claims, litigation matters and regulatory proceedings incidental to our business, including claims for damages arising out of the use of our products or services and claims relating to intellectual property matters, employment matters, commercial disputes, competition, sales and trading practices, environmental matters, personal injury, and insurance coverage. Some of these lawsuits include claims for punitive as well as compensatory damages. The defense of these lawsuits could divert our management's attention, and we could incur significant expenses in defending these lawsuits. In addition, we could be required to pay damage awards or settlements or become subject to unfavorable equitable remedies. Moreover, any insurance or indemnification rights that we could have may be insufficient or unavailable to protect us against potential loss exposures.

Our operations are consolidated primarily in one facility. A disruption at this facility could result in a prolonged interruption of our business and have a material adverse effect on our business, financial condition, and results of operations.

Substantially all of our administrative operations and our manufacturing operations are located at our facility in Irvine, California, which is near known earthquake fault zones. Although we have taken precautions to safeguard our facilities including disaster recovery planning and off-site backup of computer data, a natural disaster such as an earthquake, fire, or flood, could seriously harm our facility and significantly disrupt our operations. Additionally, labor disputes, maintenance requirements, power outages, equipment failures, civil unrest, or terrorist attacks affecting our Irvine, California facility could significantly disrupt our operations. Our business interruption insurance coverage may not cover all or any of our losses from natural disasters or other disruptions.

If we lose our key management personnel, or are unable to attract or retain qualified personnel, it could adversely affect our ability to execute our growth strategy.

Our success is dependent, in part, upon our ability to hire and retain management, engineers, marketing and sales personnel, and technical, research and other personnel who are in high demand and are often subject to competing employment opportunities. Our success will depend on our ability to retain our current personnel and to attract and retain qualified like personnel in the future. Competition for senior management, engineers, marketing and sales personnel, and other specialized technicians is intense and we may not be able to retain our personnel. If we lose the services of any executive officers or key employees, our ability to achieve our business objectives could be harmed and our business, financial condition, and results of operations could be materially and adversely affected. In general, our officers could terminate their employment at any time without notice for any reason.

Acquisitions involve risks and uncertainties, including difficulties integrating acquired businesses successfully into our existing operations and risks of discovering previously undisclosed liabilities.

Successful acquisitions depend upon our ability to identify, negotiate, complete, and integrate suitable acquisitions and to obtain any necessary financing. We expect to continue to consider opportunities to acquire or make investments in other technologies, products and businesses that could enhance our capabilities, complement our current products, or expand the breadth of our markets or customer base. We have limited experience in acquiring other businesses and technologies. Even if we complete acquisitions, we could experience:

- difficulties in integrating any acquired companies, personnel, products, and other assets into our existing business;
- delays in realizing the benefits of the acquired company, product, or other assets;
- diversion of our management's time and attention from other business concerns;
- limited or no direct prior experience in new markets or countries we could enter;
- higher costs of integration than we anticipated; and
- difficulties in retaining key employees of the acquired business.

In addition, an acquisition could cause us to incur debt or issue shares, resulting in dilution to existing stockholders. We could also discover deficiencies in internal controls, data adequacy and integrity, product quality, regulatory compliance, and product liabilities that we did not uncover prior to our acquisition of such businesses, which could result in us becoming subject to penalties or other liabilities. Any difficulties in the integration of acquired businesses or unexpected penalties or liabilities in connection with such businesses could have a material adverse effect on our business, financial condition, and results of operations.

If we fail to comply with the reporting obligations of the Exchange Act and Section 404 of the Sarbanes-Oxley Act, or if we fail to maintain adequate internal control over financial reporting, our business, financial condition, and results of operations, and investors' confidence in us, could be materially and adversely affected.

As a public company, we are required to comply with the periodic reporting obligations of the Exchange Act, including preparing annual reports, quarterly reports, and current reports. Our failure to prepare and disclose this information in a timely manner and meet our reporting obligations in their entirety could subject us to penalties under federal securities laws and regulations of The Nasdaq Stock Market LLC ("NASDAQ"), expose us to lawsuits, and restrict our ability to access financing on favorable terms, or at all.

In addition, pursuant to Section 404 of the Sarbanes-Oxley Act, we are required to evaluate and provide a management report of our systems of internal control over financial reporting. During the course of the evaluation of our internal control over financial reporting, we could identify areas requiring improvement and could be required to design enhanced processes and controls to address issues identified through this review. This could result in significant delays and costs to us and require us to divert substantial resources, including management time, from other activities. In addition, if we fail to maintain the adequacy of our internal control over financial reporting, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with the Sarbanes-Oxley Act. Moreover, effective internal controls are necessary for us to produce reliable financial reports and are important to help prevent fraud. Any failure to maintain compliance with the requirements of Section 404 on a timely basis could result in the loss of investor confidence in the reliability of our financial statements, which in turn could, negatively impact the trading price of our stock, and adversely affect investors' confidence in the Company and our ability to access capital markets for financing.

Climate change initiatives could materially and adversely affect our business, financial condition, and results of operations.

Our manufacturing processes require that we purchase significant quantities of energy from third parties, which results in the generation of greenhouse gases, either directly on-site or indirectly at electric utilities. Both domestic and international legislation to address climate change by reducing greenhouse gas emissions and establishing a price on carbon could create increases in energy costs and price volatility. Considerable international attention is now focused on development of an international policy framework to address climate change. Proposed and existing legislative efforts to control or limit greenhouse gas emissions could affect our energy source and supply choices as well as increase the cost of energy and raw materials derived from sources that generate greenhouse gas emissions. If our suppliers are unable to obtain energy at a reasonable cost in the future, the cost of our raw materials could be negatively impacted which could result in increased manufacturing costs.

Risks Related to Our Intellectual Property

If the patents that we own or license, or our other intellectual property rights, do not adequately protect our technologies, we could lose market share to our competitors and be unable to operate our business profitably.

Our future success depends, in part, on our ability to obtain and maintain patent protection for our products and technology, to preserve our trade secrets and to operate without infringing the intellectual property of others. We rely on patents to establish and maintain proprietary rights in our technology and products. We currently possess a number of issued patents and patent applications with respect to our products and technology. However, we cannot ensure that any additional patents will be issued, that the scope of any patent protection will be effective in helping us address our competition, or that any of our patents will be held valid if subsequently challenged. It is also possible that our competitors could independently develop similar or more desirable products, duplicate our products, or design products that circumvent our patents. The laws of foreign countries may not protect our products or intellectual property rights to the same extent as the laws of the United States. In addition, there have been recent changes in the patent laws and rules of the U.S. Patent and Trademark Office (the "USPTO"), and there could be future proposed changes that, if enacted, have a significant impact on our ability to protect our technology and enforce our intellectual property rights. If we fail to protect our intellectual property rights adequately, our competitive position could be adversely affected, and there could be a material adverse effect on our business, financial condition, and results of operations.

If third parties claim that we infringe their intellectual property rights, we could incur liabilities and costs and have to redesign or discontinue selling certain products, which could have a material adverse effect on our business, financial condition, and results of operations.

We face substantial uncertainty regarding the impact that other parties' intellectual property positions will have on dental and other medical laser applications. The medical technology industry has in the past been characterized by a substantial amount of litigation and related administrative proceedings regarding patents and intellectual property rights. From time to time, we have received, and we expect to continue to receive, notices of claims of infringement, misappropriation, or misuse of other parties' proprietary rights. Some of these claims could lead to litigation. We may not prevail in any future intellectual property infringement litigation given the complex technical issues and inherent uncertainties in litigation. Any claims, with or without merit, could be time-consuming and distracting to management, result in costly litigation, or cause product shipment delays. Adverse determinations in litigation could subject us to significant liability and could result in the loss of proprietary rights. A successful lawsuit against us could also force us to cease selling or redesign products that incorporate the infringed intellectual property. Additionally, we could be required to seek a license from the holder of the intellectual property to use the infringed technology, and we may not be able to obtain a license on acceptable terms, or at all.

Risks Related to Our Regulatory Environment

Changes in government regulation or the inability to obtain or maintain necessary government approvals could have a material adverse effect on our business, financial condition, and results of operations.

Our products are subject to extensive government regulation, both in the United States and in other countries. To clinically test, manufacture, and market products for human use, we must comply with regulations and safety standards set by the FDA and comparable state and foreign agencies. Regulations adopted by the FDA are wide-ranging and govern, among other things, product design, development, manufacture and control testing, labeling control, storage, advertising, and sales. Generally, products must meet regulatory standards as safe and effective for their intended use before being marketed for human applications. The clearance process is expensive, time-consuming, and uncertain. Failure to comply with applicable regulatory requirements of the FDA can result in an enforcement action, which could include a variety of sanctions, including fines, injunctions, civil penalties, recall or seizure of our products, operating restrictions, partial suspension, or total shutdown of production and criminal prosecution. The failure to receive or maintain requisite approvals for the use of our products or processes, or significant delays in obtaining such approvals, could prevent us from developing, manufacturing, and marketing products and services necessary for us to remain competitive.

If we develop new products and applications or make any significant modifications to our existing products or labeling, we will need to obtain additional regulatory clearances or approvals. Any modification that could significantly affect a product's safety or effectiveness, or that would constitute a change in its intended use, will require a new FDA 510(k) clearance, or could require a PMA application. The FDA requires each manufacturer to make this determination initially, but the FDA can review any such decision and can disagree with a manufacturer's determination. If the FDA disagrees with a manufacturer's determination, the FDA can require the manufacturer to cease marketing and/or recall the modified device until 510(k) clearance or PMA is obtained. If 510(k) clearance is denied and a PMA application is required, we could be required to submit substantially more data and conduct human clinical testing and would very likely be subject to a significantly longer review period.

Products sold in international markets are also subject to the regulatory requirements of each respective country or region. The regulations of the European Union require that a device have a CE Mark, indicating conformance with European Union laws and regulations before it can be sold in the European Union. The regulatory international review process varies from country to country. We rely on our distributors and sales representatives in the foreign countries in which we market our products to comply with the regulatory laws of such countries. Failure to comply with the laws of such countries could prevent us from continuing to sell products in such countries. In addition, unanticipated changes in existing regulatory requirements or the adoption of new requirements could impose significant costs and burdens on us, which could increase our operating expenses.

Changes in health care regulations in the U.S. and elsewhere could adversely affect the demand for our products as well as the way in which we conduct our business. For example, in 2010, President Obama signed the Affordable Care Act into law, which included various reforms impacting Medicare coverage and reimbursement, including revision to prospective payment systems, any of which could adversely impact any Medicare reimbursements received by our end-user customers. New legislation may be enacted as President Trump and Congress consider further reform. In addition, as a result of the focus on health care reform, there is risk that Congress could implement changes in laws and regulations governing health care service providers, including measures to control costs, and reductions in reimbursement levels. We cannot be sure that government or private third-party payers will cover and reimburse the procedures using our products, in whole or in part, in the future, or that payment rates will be adequate. If providers cannot obtain adequate coverage and reimbursement for our products, or the procedures in which they are used, our business, results of operations, and financial condition could suffer.

We could be subject to or otherwise affected by federal and state health care laws, including fraud and abuse and health information privacy and security laws, and we could face substantial penalties if we are unable to fully comply with such regulations.

We are directly or indirectly, through our customers, subject to extensive regulation by both the federal government and the states and foreign countries in which we conduct our business. The laws that directly or indirectly affect our ability to operate our business include, but are not limited to, the following:

- the Federal Food, Drug, and Cosmetic Act, which regulates the design, testing, manufacture, labeling, marketing, distribution, and sale of prescription drugs and medical devices and which includes the RCHSA, under which the FDA has established reporting, recordkeeping, and performance requirements for laser products;
- state food and drug laws;

- the federal Anti-Kickback Statute, which prohibits persons from knowingly and willfully soliciting, offering, receiving, or providing remuneration, directly or indirectly, to induce the referral for the furnishing of, or the purchase, order, or recommendation of, a good or service, for which payment could be made under FHCPS such as Medicare, Medicaid, and TRICARE;
- state law equivalents to the federal Anti-Kickback Statute, which may not be limited to government reimbursed items;
- state laws that prohibit fee-splitting arrangements;
- the federal Civil False Claims Act, which imposes liability on any person or entity that knowingly presents, or causes to be presented, a false or fraudulent claim for payment to the government, including FHCPS;
- state false claims laws that prohibit anyone from presenting, or causing to be presented, claims for payment to third-party payers that are false or fraudulent;
- federal crimes for knowingly and willfully executing a scheme to defraud any health care benefit program or making false statements in connection with the delivery of or payment for items or services under a health care benefit program;
- federal law prohibiting offering remuneration to a Medicare or Medicaid beneficiary to influence the beneficiary's selection of a particular provider, practitioner, or supplier;
- the federal Stark Law, which, in the absence of a statutory or regulatory exception, prohibits: (i) the referral of Medicare or Medicaid patients by a physician to an entity for the provision of designated health care services, if the physician or a member of the physician's immediate family has a direct or indirect financial relationship, including an ownership interest in, or a compensation arrangement with, the entity and (ii) submitting a bill to Medicare or Medicaid for services rendered pursuant to a prohibited referral;
- state law equivalents to the Stark Law, which may not be limited to government reimbursed items;
- the Physician Payments Sunshine Act, which requires us to report annually to CMS certain payments and other transfers of value we make to U.S.-licensed physicians, dentists, and teaching hospitals;
- the FCPA, which generally prohibits companies and their intermediaries from paying anything of value to foreign officials to influence any decision of the foreign official in his/her official capacity or to secure any other improper advantage to obtain or retain business;
- HIPAA and HITECH and their implementing regulations, which govern the use, disclosure, and safeguarding of PHI;
- state privacy laws that protect the confidentiality of patient information;
- Medicare and Medicaid laws and regulations that prescribe the requirements for coverage and payment, including the amount of such payment; state laws that prohibit the practice of medicine by non-physicians; and
- the Federal Trade Commission Act and similar laws regulating advertising and consumer protection.

If our past or present operations are found to be in violation of any of the laws described above or the other governmental laws or regulations to which we or our customers are subject, we could be subject to the applicable penalty associated with the violation, which could include civil and criminal penalties, damages, fines, exclusion from FHCPS, and the curtailment or restructuring of our operations. If we are required to obtain permits or licensure under these laws that we do not already possess, we could become subject to substantial additional regulation or incur significant expense. Any penalties, damages, fines, or curtailment or restructuring of our operations could be significant. The risk of potential non-compliance is increased by the fact that many of these laws have not been fully interpreted by applicable regulatory authorities or the courts, and their provisions are open to a variety of interpretations and additional legal or regulatory change. Any action against us for violation of these laws, even if we successfully defend against it, could cause us to incur significant legal expenses, divert our management's attention from the operation of our business, damage our reputation, and cause a material adverse effect on our business, financial condition, and results of operations.

We could be exposed to liabilities under the FCPA, and any determination that we violated the FCPA could have a material adverse effect on our business, financial condition, and results of operations.

In light of our operations outside the United States, we are subject to the FCPA, which generally prohibits companies and their intermediaries from offering to pay, promising to pay, or authorizing the payment of money or anything of value to non-U.S. officials for the purpose of influencing any act or decision of the foreign official in his/her capacity or to secure any other improper advantage to obtain or retain business. Violation of the anti-bribery provisions of the FCPA can result in criminal fines of up to \$2 million and civil penalties of up to \$16,000 for each violation. Individuals, including officers, directors, stockholders, and agents of companies, can be subject to a criminal fine of up to \$250,000 and imprisonment, in addition to civil penalties of up to \$16,000, per violation. We could be held liable for actions taken by our distributors in violation of the FCPA, even though such partners are foreign companies that may not be subject to the FCPA. Any determination that we violated the FCPA could result in sanctions that could have a material adverse effect on our business, financial condition, and results of operations.

Product sales or introductions could be delayed or canceled as a result of the FDA regulatory requirements applicable to laser products, dental devices, or both, which could cause our sales or profitability to decline and have a material adverse effect on our business, financial condition, and results of operations.

The process of obtaining and maintaining regulatory approvals and clearances to market a medical device from the FDA and similar regulatory authorities abroad can be costly and time-consuming, and we cannot provide assurance that such approvals and clearances will be granted. Pursuant to FDA regulations, unless exempt, the FDA permits commercial distribution of a new medical device only after the device has received 510(k) clearance or is the subject of an approved PMA. The FDA will clear marketing of a medical device through the 510(k) process if it is demonstrated that the new product is substantially equivalent to other 510(k)-cleared products. The PMA process is more costly, lengthy and uncertain than the 510(k) process, and must be supported by extensive data, including data from preclinical studies, and human clinical trials. Because we cannot provide assurance that any new products, or any product enhancements, that we develop will be subject to the shorter 510(k) clearance process, significant delays in the introduction of any new products or product enhancement could occur. We cannot provide assurance that the FDA will not require a new product or product enhancement to go through the lengthy and expensive PMA process. Delays in obtaining regulatory clearances and approvals could:

- delay or eliminate commercialization of products we develop;
- require us to perform costly procedures;
- diminish any competitive advantages that we may attain; and
- reduce our ability to collect revenues or royalties.

Although we have obtained 510(k) clearance from the FDA to market our dental laser systems, we cannot provide assurance that we will not be required to obtain new clearances or approvals for modifications or improvements to our products.

Our products are subject to recalls and other regulatory actions after receiving FDA clearance or approval.

The FDA and similar governmental bodies in other countries have the authority to require the recall of our products in the event of material deficiencies or defects in design or manufacture. A government mandated or voluntary recall by us could occur as a result of component failures, manufacturing errors, or design defects, including defects in labeling. Any recall would divert management's attention and financial resources and harm our reputation with customers. Any recall involving our laser systems would be particularly harmful to us, because our laser systems comprise such an important part of our portfolio of products. However, any recall could have a material adverse effect on our business, financial condition, and results of operations.

Risks Related to Our Stock

The liquidity and trading volume of our common stock could be low, and our ownership is concentrated.

The liquidity and trading volume of our common stock has at times been low in the past and could again be low in the future. If the liquidity and trading volume of our common stock is low, this could adversely impact the trading price of our shares, our ability to issue stock and our stockholders' ability to obtain liquidity in their shares. The issuance of common stock by us in 2013, 2014, 2016 and 2017 involved a significant issuance of stock to a limited number of investors, significantly increasing the concentration of our share ownership in a few holders.

Two of our stockholders beneficially own approximately 62% of our outstanding common stock, in the aggregate, as of December 31, 2017, as determined based on a review of their reports on Schedule 13D/A. As a result, these stockholders will be able to affect the outcome of, or exert significant influence over, all matters requiring stockholder approval, including the election and removal of directors and any change in control. In particular, this concentration of ownership of our common stock could have the effect of delaying or preventing a change in control of us or otherwise discouraging or preventing a potential acquirer from attempting to obtain control of us. This, in turn, could have a negative effect on the market price of our common stock. It could also prevent our stockholders from realizing a premium over the market prices for their shares of common stock. Moreover, the interests of this concentration of ownership may not always coincide with our interests or the interests of other stockholders. The concentration of ownership also contributes to the low trading volume and volatility of our common stock.

Our stock price has been, and could continue to be, volatile.

There has been significant volatility in the market price and trading volume of equity securities, which is often unrelated to the financial performance of the companies issuing the securities. These broad market fluctuations could negatively affect the market price of our stock. The market price and volume of our common stock could fluctuate, and in the past has fluctuated, more dramatically than the stock market in general. You may not be able to resell your shares at or above the price you paid for them due to fluctuations in the market price of our stock caused by changes in our operating performance or prospects or other factors. Some factors, in addition to the other risk factors identified above, that could have a significant effect on our stock market price include but are not limited to the following:

- actual or anticipated fluctuations in our operating results or future prospects;
- our announcements or our competitors' announcements of new products;
- the public's reaction to our press releases, our other public announcements, and our filings with the SEC;
- strategic actions by us or our competitors, such as acquisitions or restructurings;
- new laws or regulations or new interpretations of existing laws or regulations applicable to our business;
- changes in accounting standards, policies, guidance, interpretations, or principles;
- changes in our growth rates or our competitors' growth rates;
- developments regarding our patents or proprietary rights or those of our competitors;
- our inability to raise additional capital as needed;
- concerns or allegations as to the safety or efficacy of our products;
- changes in financial markets or general economic conditions;
- sales of stock by us or members of our management team, our Board, our significant stockholders, or certain institutional stockholders; and
- changes in stock market analyst recommendations or earnings estimates regarding our stock, other comparable companies or our industry generally.

Our common stock may be subject to delisting from the NASDAQ Capital Market.

On August 9, 2017, we received a letter from the staff of NASDAQ notifying us that we violated the continued listing requirements of NASDAQ listing rule 5550(a)(2). As provided in the NASDAQ rules, we had 180 calendar days, or until February 5, 2018, to submit a plan to regain compliance, which plan was submitted prior to February 5, 2018.

On February 6, 2018, as a result of our submission of a plan to regain compliance, we were granted an additional 180 days to regain compliance. However the letter stated that if we were to fail to regain compliance during the additional compliance period, we may be subject to delisting.

If subsequent to the filing of this Annual Report on Form 10-K for the year ended December 31, 2017, we receive written notification from staff of NASDAQ notifying us of potential delisting due to non-compliance with the continued listing requirements of NASDAQ listing rule 5500(a)(2), we intend to appeal the delisting notice to the NASDAQ hearings panel, and develop a plan to satisfy the requirement to reach compliance and to continue listing on the NASDAQ Capital Market. We cannot guarantee that we will be able to develop such a plan or, if we are able to do so, that NASDAQ would accept it. If we cannot develop a plan, or if we do, and it is not accepted, or if we are not granted an extension, then our common stock could be delisted from The NASDAQ Capital Market. If our common stock is delisted, this would, among other things, substantially impair our ability to raise additional funds and could result in a loss of institutional investor interest and fewer development opportunities for us.

You could experience substantial dilution of your investment as a result of subsequent exercises of our outstanding warrants and options, future sales of our equity, or the future grant of equity by us.

You could experience substantial dilution of your investment as a result of subsequent exercises of outstanding warrants and outstanding options issued as compensation for services performed by employees, directors, consultants, and others, warrants issued in past sales of our equity, future sales of our equity, or the grant of future equity-based awards. During 2017, we sold approximately 34.4 million shares of common stock in a rights offering and private placement with gross proceeds totaling approximately \$22.5 million. During 2016, we sold approximately 0.9 million shares of common stock in private placements with gross proceeds totaling approximately \$10.0 million. We did not complete any private placements during 2015. During 2014, we sold approximately 22.4 million shares of common stock in private placements with gross proceeds totaling approximately \$52.0 million.

As of December 31, 2017, an aggregate of 15,550,000 shares of common stock were reserved for issuance under our equity incentive plan, 6,737,257 of which were subject to options outstanding as of that date at a weighted-average exercise price of \$1.80 per share. In addition, as of December 31, 2017, 6,126,269 shares of our common stock were subject to warrants at a weighted-average exercise price of \$1.93 per share. Of the 6,737,257 stock options outstanding at December 31, 2017, 3,453,922 stock options were vested and exercisable. To the extent that outstanding warrants or options are exercised, our existing stockholders could experience dilution. We rely heavily on equity awards to motivate current employees and to attract new employees. The grant of future equity awards by us to our employees and other service providers could further dilute our stockholders' interests in the Company.

Anti-takeover provisions in our charter, bylaws, other agreements, and under Delaware law could discourage, delay, or prevent a change in control of the Company.

Provisions in our restated certificate of incorporation and amended and restated bylaws could discourage, delay, or prevent a merger or acquisition involving us that our stockholders may consider favorable. These provisions include but are not limited to the right of our Board to issue preferred stock without stockholder approval, no stockholder ability to fill director vacancies, elimination of the rights of our stockholders to act by written consent and call special stockholder meetings, super-majority vote requirements for certain amendments to our certificate of incorporation and stockholder proposals for amendments to our bylaws, prohibition against stockholders from removing directors other than "for cause" and rules regarding how stockholders may present proposals or nominate directors for election at stockholder meetings.

We are also subject to the anti-takeover provisions of the Delaware General Corporation Law. Under these provisions, if anyone becomes an "interested stockholder," we may not enter into a "business combination" with that person for three years without special approval, which could discourage a third-party from making a takeover offer and could delay or prevent a change in control of us. An "interested stockholder" generally means (subject to certain exceptions as described in the Delaware General Corporation Law) someone owning 15% or more of our outstanding voting stock or an affiliate of ours that owned 15% or more of our outstanding voting stock during the past three years.

On November 10, 2015, we entered into Standstill Agreements with certain stockholders, and on August 1, 2016 and November 9, 2017, we amended the Standstill Agreements. As amended, the Standstill Agreements restrict certain stockholders from (i) purchasing or acquiring any shares of BIOLASE common stock if such a purchase would result in aggregate beneficial ownership in excess of 41% of the issued and outstanding shares of BIOLASE common stock and (ii) selling, transferring or otherwise conveying shares of BIOLASE common stock (or warrants or other rights to acquire shares of BIOLASE common stock) to anyone who would immediately thereafter beneficially own shares in excess of 20% of the issued and outstanding shares of BIOLASE common stock, as a result of such transfer and other transfers from third parties. These Standstill Agreements may discourage, delay, or prevent a change in control of the Company.

Because we do not intend to pay dividends, our stockholders will benefit from an investment in our common stock only if it appreciates in value.

We intend to retain our future earnings, if any, to finance the expansion of our business and do not expect to pay any cash dividends in the foreseeable future. As a result, the success of an investment in our common stock will depend entirely upon any future appreciation. There is no guarantee that our common stock will appreciate in value or even maintain the price at which our stockholders purchased their shares.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

As of December 31, 2017, we owned or leased a total of approximately 74,000 square feet of space worldwide. We lease our corporate headquarters and manufacturing facility, which consists of approximately 57,000 square feet in Irvine, California. Our lease expires on April 30, 2020. We also own a 12,000 square foot manufacturing and administrative facility in Floss, Germany. See Note 3 to the *Notes to the Consolidated Financial Statements — Supplementary Balance Sheet Information — Property, Plant, and Equipment, Net*.

We believe that our current facilities are sufficient for the current operations of our business, and we believe that suitable additional space in various applicable local markets is available to accommodate any needs that may arise.

Item 3. Legal Proceedings

From time to time, we are involved in legal proceedings and regulatory proceedings arising out of our operations. We establish reserves for specific liabilities in connection with legal actions that we deem to be probable and estimable. The ability to predict the ultimate outcome of such matters involves judgments, estimates, and inherent uncertainties. The actual outcome of such matters could differ materially from management's estimates.

Intellectual Property Litigation

On April 24, 2012, CAO Group, Inc. ("CAO") filed a lawsuit against BIOLASE in the District of Utah alleging that BIOLASE's ezlase dental laser infringes on U.S. Patent No. 7,485,116 (the "116 Patent"). On September 9, 2012, CAO amended its complaint, adding claims for (1) business disparagement/injurious falsehood under common law and (2) unfair competition under 15 U.S.C. Section 1125(a). The additional claims stem from a press release that BIOLASE issued on April 30, 2012, which CAO claims contained false statements that are disparaging to CAO and its diode product. The amended complaint seeks injunctive relief, treble damages, attorneys' fees, punitive damages, and interest. Until January 24, 2018, this lawsuit was stayed in connection with United States Patent and Trademark Office proceedings relating to the 116 Patent, which proceedings ultimately culminated in a January 27, 2017 decision by the United States Court of Appeals for the Federal Circuit, affirming the findings of the Patent Trial and Appeal Board, which were generally favorable to the Company. On January 25, 2018, CAO moved for leave to file a second amended complaint to add certain claims, which filing the Company is not opposing.

On January 23, 2018, CAO filed a lawsuit against BIOLASE in the Central District of California alleging that BIOLASE's diode lasers infringe on U.S. Patent Nos. 8,337,097, 8,834,497, 8,961,040 and 8,967,883. The complaint seeks injunctive relief, treble damages, attorneys' fees, punitive damages, and interest.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

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

Market Information

Our common stock is traded on the NASDAQ Capital Market under the symbol "BIOL."

The following table sets forth the high and low closing prices for our common stock for the periods indicated:

	2017		2016	
	High	Low	High	Low
First Quarter	\$ 1.70	\$ 1.15	\$ 1.60	\$ 0.75
Second Quarter	\$ 1.40	\$ 0.94	\$ 1.44	\$ 1.00
Third Quarter	\$ 0.98	\$ 0.49	\$ 1.93	\$ 0.93
Fourth Quarter	\$ 0.75	\$ 0.39	\$ 1.84	\$ 1.28

The above quotations reflect inter-dealer prices, without retail markup, markdown, or commission and may not necessarily represent actual transactions.

As of March 7, 2018, the closing price of our common stock on the NASDAQ Capital Market was \$0.44 per share, and the number of stockholders of record was approximately 170. We believe that the number of beneficial owners is substantially greater than the number of record holders because a large portion of our stock is held of record through brokerage firms in “street name.”

Dividend Policy

We intend to retain our available funds from earnings and other sources for future growth and, therefore, do not anticipate paying any cash dividends in the foreseeable future. Additionally, we do not anticipate paying any stock dividends in 2018. Our dividend policy may be changed at any time, and from time to time, by our Board. We did not pay or declare any dividends in 2016 or 2017.

Equity Compensation Plan Information

Our 2002 Stock Incentive Plan, as amended (the “2002 Stock Incentive Plan”) is designed to attract and retain the services of individuals essential to the Company’s long-term growth and success. The following table summarizes information as of December 31, 2017 with respect to the shares of our common stock that may be issued upon exercise of options, warrants or rights under our 2002 Stock Incentive Plan.

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options and release of Restricted Stock Units	Weighted Average Exercise Price of Outstanding Options	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding securities reflected in column)
Equity Compensation Plans Approved by Stockholders	8,526,388	\$ 1.80	3,059,916
Equity Compensation Plans Not Approved by Stockholders	—	—	—
Total	8,526,388	\$ 1.80	3,059,916

Item 6. Selected Financial Data

None

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

The following information should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this Form 10-K. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties, and assumptions, which could cause actual results to differ materially from management's expectations. Please see the "Cautionary Statement Regarding Forward-Looking Statements" section immediately preceding Part I, Item 1 of this Form 10-K and the "Risk Factors" section in Part I, Item 1A of this Form 10-K.

Overview

We are a medical device company that develops, manufactures, markets, and sells laser systems in dentistry and medicine and also markets, sells, and distributes dental imaging equipment, including three-dimensional CAD/CAM intra-oral scanners and digital dentistry software. Our products advance the practice of dentistry and medicine for patients and health care professionals. Our proprietary dental laser systems allow dentists, periodontists, endodontists, oral surgeons, and other dental specialists to perform a broad range of minimally invasive dental procedures, including cosmetic, restorative, and complex surgical applications. Our laser systems are designed to provide clinically superior results for many types of dental procedures compared to those achieved with drills, scalpels, and other conventional instruments. We have clearance from the FDA to market and sell our laser systems in the United States and also have the necessary registration to market and sell our laser systems in Canada, the European Union, and many other countries outside the United States. Additionally, our in-licensed imaging equipment and related products improve diagnoses, applications, and procedures in dentistry and medicine.

We offer two categories of laser system products: Waterlase (all-tissue) systems and Diode (soft-tissue) systems. Our flagship brand, the Waterlase, uses a patented combination of water and laser energy to perform most procedures currently performed using drills, scalpels, and other traditional dental instruments for cutting soft and hard tissue. We also offer our Diode laser systems to perform soft tissue, pain therapy, and cosmetic procedures, including teeth whitening. We have approximately 220 issued and 95 pending U.S. and international patents, the majority of which are related to Waterlase technology. From 1998 through December 31, 2017, we sold over 36,200 laser systems in over 90 countries around the world. Contained in this total are approximately 12,400 Waterlase systems, including approximately 8,400 Waterlase MD, MDX, Express and iPlus systems.

Consistent with our goal to focus our energies on strengthening our leadership, and worldwide competitiveness and increasing the amount of attention we pay to our professional customers and their patients, we have made strategic personnel additions to our senior management team. In September 2017, we named Jonathan T. Lord, M.D. as our new Chairman of the Board. Dr. Lord has served on our Board since 2014 and also serves as Chairman of the Compensation Committee and a member of the Nominating and Corporate Governance Committee. He is a board-certified forensic pathologist and Fellow of the College of American Pathologists. Dr. Lord brings extensive innovation, executive management and board experience to his new role of Chairman. On October 1, 2017, we appointed a new Senior Vice President and Chief Financial Officer with proven leadership and technical experience in finance and business management in both public and private companies. On November 1, 2017, we appointed Richard B. Lanman, M.D. to our Board, a well-known healthcare innovator and entrepreneur who specializes in the development and adoption of novel healthcare technologies. In January, we promoted from within a new Vice President of U.S. Sales, with a wealth of experience and knowledge about our Company and the industry.

In December 2017, we completed a rights offering with holders of our common stock as of the record date of 5:00 p.m., Eastern Time on November 8, 2017. Gross proceeds from the sale were \$12.0 million, and net proceeds, after offering expenses of approximately \$0.6 million, were approximately \$11.4 million. In April 2017, we completed a private placement with several institutional and individual investors, and certain of our directors and officers. Gross proceeds from the sale were \$10.5 million, and net proceeds, after offering expenses of approximately \$0.3 million, were approximately \$10.2 million.

In February 2017, we launched the fifth-generation Waterlase Express all-tissue laser system. Waterlase Express represents the newest addition to our Waterlase portfolio of Er,Cr:YSGG all-tissue lasers. Waterlase Express was exhibited at the Chicago Dental Society's Mid-Winter meeting in February 2017. Designed for easy and intuitive operation, integrated learning, and portability, Waterlase Express is our next-generation Waterlase system. Waterlase Express has regulatory clearance for commercial distribution from the FDA, and is available for sale to dentists in the U.S. as well as select international markets in Europe, the Middle East, and Asia.

In January 2017, we received FDA clearance and launched Epic Pro, a powerful and innovative dental diode laser system, making it available for sale in the U.S., as well as in select countries in Europe, the Middle East, and Asia. The Epic Pro, which offers more power than most diode lasers in dentistry, is the first product to be introduced resulting from our strategic development agreement with IPG Medical. The newest addition to the Epic family of dental soft-tissue lasers, Epic Pro features several new innovations, such as a new super pulse technology for more precise, enhanced laser tissue cutting; real-time automatic power control to enhance speed and consistency when performing surgery; and pre-initiated, bendable, disposable tips with new smart tip technology to ensure tip performance and quality. The Epic Pro laser system has FDA clearance for dental and surgical operations, intended for use in contact and non-contact techniques for incision, excision, vaporization, ablation, hemostasis, or coagulation of intraoral and extra-oral soft tissue (including marginal and interdental gingiva and epithelial lining of free gingiva).

In summary, 2017 was a year of continued transformation for BIOLASE, positioning the Company in executing on our strategic goals of returning BIOLASE to a successful growing company and continuing as the clear worldwide industry leader in the dental laser segment. Although we have made improvements throughout the year, it will take time for the financial statements to reflect the changes and as such, for the three years ended December 31, 2017 we have reported recurring losses from operations and have not generated cash from operations. Our level of cash used in operations, the potential need for additional capital, and the uncertainties surrounding our ability to raise additional capital, raise substantial doubt about our ability to continue as a going concern. As a result, the opinion we have received from our independent registered public accounting firm, on our consolidated financial statements, contains an explanatory paragraph stating that there is a substantial doubt regarding our ability to continue as a going concern.

The accompanying financial statements have been prepared on a going concern basis, which assumes that we will continue in operation for the next 12 months and will be able to realize our assets and discharge our liabilities and commitments in the normal course of business. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Critical Accounting Policies

The preparation of consolidated financial statements and related disclosures in conformity with generally accepted accounting principles in the United States (“GAAP”) requires us to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and the accompanying notes. The following is a summary of those accounting policies that we believe are necessary to understand and evaluate our reported financial results.

Revenue Recognition. We sell our products in North America directly to customers through our field sales force and through non-exclusive distributors. We sell our products internationally through exclusive and non-exclusive distributors as well as directly to customers in certain countries. Sales are recorded upon shipment from our facility, and payment of our invoices is generally due within 90 days or less. Internationally, we primarily sell products through independent distributors. We record revenue based on four basic criteria that must be met before revenue can be recognized: (i) persuasive evidence of an arrangement exists; (ii) delivery has occurred and title and the risks and rewards of ownership have been transferred to our customer, or services have been rendered; (iii) the price is fixed or determinable; and (iv) collectability is reasonably assured. Revenue is recorded for all sales upon shipment assuming all other revenue recognition criteria are met.

Sales of our laser systems include separate deliverables consisting of the product, disposables used with the laser systems, installation, and training. For sale of deliverables that are part of a multiple-element arrangement, we apply a method that approximates the relative selling price method, which requires that arrangement consideration be allocated at the inception of an arrangement to all deliverables using the relative selling price method. This requires us to use estimated selling prices of each of the deliverables in the total arrangement. The sum of those prices is then compared to the arrangement, and any difference is applied to the separate deliverable ratably. This method also establishes a selling price hierarchy for determining the selling price of a deliverable, which includes: (i) vendor-specific objective evidence (“VSOE”), if available, (ii) third-party evidence if VSOE is not available, and (iii) estimated selling price if neither VSOE nor third-party evidence is available. VSOE is determined based on the value we sell the undelivered element to a customer as a stand-alone product. Revenue attributable to the undelivered elements is included in deferred revenue when the product is shipped and is recognized when the related service is performed. Disposables not shipped at time of sale and installation services are typically shipped or installed within 30 days. Training is included in deferred revenue when the product is shipped and is recognized when the related service is performed or upon the appropriate expiration of time offered under the agreement.

Key judgments related to our revenue recognition include the collectability of payment from the customer, the satisfaction of all elements of the arrangement having been delivered, and that no additional customer credits and discounts are needed. We evaluate a customer’s credit worthiness prior to the shipment of the product. Based on our assessment of the available credit information, we may determine the credit risk is higher than normally acceptable, and we will either decline the purchase or defer the revenue until payment is reasonably assured. Future obligations required at the time of sale may also cause us to defer the revenue until the obligation is satisfied.

Although all sales are final, we accept returns of products in certain, limited circumstances and record a provision for sales returns based on historical experience concurrent with the recognition of revenue. The sales returns allowance is recorded as a reduction of accounts receivable and revenue.

Extended warranty contracts, which are sold to our laser and certain imaging customers, are recorded as revenue on a straight-line basis over the period of the contracts, which is typically one year.

For sales transactions involving used laser trade-ins, we record the purchased trade-ins as inventory at the fair value of the asset surrendered with the offset to accounts receivable. In determining the estimated fair value of used laser trade-ins, we assess usable parts and key components and consider the ultimate resale value of the certified pre-owned (or "CPO") laser with applicable margins. We sell these CPO laser trade-ins as refurbished lasers. Trade-in rights are not established or negotiated with customers during the initial sales transaction of the original lasers. Trade-in rights are promotional events used at our discretion to encourage existing laser customers to purchase new lasers. A customer is not required to trade in a laser nor are we required to accept a trade-in. However, the promotional value offered in exchange for the trade-in laser is not offered without a laser trade-in. The transaction is treated as a monetary transaction as each sale transaction involving a customer trade-in includes significant boot of greater than 25% of the fair value of the exchange. As a monetary transaction, the sale is recognized following our laser system revenue recognition policy. There have been no sales transactions in which the cash consideration was less than 25% of the total transaction value.

We recognize revenue for royalties under licensing agreements for our patented technology when the product using our technology is sold. We estimate and recognize the amount earned based on historical performance and current knowledge about the business operations of our licensees. Our estimates have been consistent with amounts historically reported by the licensees. Licensing revenue related to exclusive licensing arrangements is recognized concurrent with the related exclusivity period.

From time to time, we may offer sales incentives and promotions on our products. We record the cost of sales incentives at the date at which the related revenue is recognized as a reduction in revenue, an increase in cost of goods sold, or a selling expense, as applicable, or later, in the case of incentives offered after the initial sale has occurred.

Accounting for Stock-Based Payments. We recognize compensation cost related to all stock-based payments based on the grant-date fair value using the Black-Scholes option valuation model, taking into consideration the probability of vesting and estimated forfeitures.

Valuation of Accounts Receivable. We maintain an allowance for uncollectible accounts receivable to estimate the risk of extending credit to customers. We evaluate our allowance for doubtful accounts based upon our knowledge of customers and their compliance with credit terms. The evaluation process includes a review of customers' accounts on a regular basis, which incorporates input from sales, service, and finance personnel. The review process also evaluates all account balances with amounts past due and other specific amounts for which information obtained indicates that the balance may be uncollectible. The allowance for doubtful accounts is adjusted based on such evaluation, with a corresponding provision included in general and administrative expenses. Account balances are charged off against the allowance when we believe it is probable the receivable will not be recovered. We do not have any off-balance-sheet credit exposure related to our customers.

Valuation of Inventory. Inventory is valued at the lower of cost or net realizable value, with cost determined using the first-in, first-out method. We periodically evaluate the carrying value of inventory and maintain an allowance for excess and obsolete inventory to adjust the carrying value as necessary to the lower of cost or market. We evaluate quantities on hand, physical condition, and technical functionality, as these characteristics may be impacted by anticipated customer demand for current products and new product introductions. Unfavorable changes in estimates of excess and obsolete inventory would result in an increase in cost of revenue and a decrease in gross profit.

Valuation of Long-Lived Assets. Property, plant, and equipment and certain intangibles with finite lives are amortized over their estimated useful lives. Useful lives are based on our estimate of the period that the assets will generate revenue or otherwise productively support our business goals. We monitor events and changes in circumstances that could indicate that the carrying balances of long-lived assets may exceed the undiscounted expected future cash flows from those assets. If such a condition were to exist, we would determine if an impairment loss should be recognized by comparing the carrying amount of the assets to their fair value.

Valuation of Goodwill and Other Intangible Assets. Goodwill and other intangible assets with indefinite lives are not subject to amortization but are evaluated for impairment annually or whenever events or changes in circumstances indicate that the asset might be impaired. We conducted our annual impairment analysis of our goodwill as of June 30, 2017 and concluded there had been no impairment in goodwill. We closely monitor our stock price and market capitalization and perform such analysis when events or circumstances indicate that there may have been a change to the carrying value of those assets.

Warranty Cost. We provide warranties against defects in materials and workmanship of our laser systems for specified periods of time. For the years ended December 31, 2017, 2016, and 2015 laser systems sold domestically were covered by our warranty for a period of up to two years from the date of sale by us or the distributor to the end-user. In 2017, for Waterlase systems sold domestically and purchased in 2017 or later, we decreased the warranty period from two years to one year. Laser systems sold internationally were covered by our warranty for a period of up to 28 months from the date of sale to the international distributor. In 2017, for Waterlase systems sold internationally and purchased in 2017 or later, we decreased the warranty period from 28 months to 16 months. Estimated warranty expenses are recorded as an accrued liability with a corresponding provision to cost of revenue. This estimate is recognized concurrent with the recognition of revenue on the sale to the distributor or end-user. Warranty expenses expected to be incurred after one year from the time of sale to the distributor are classified as a long-term warranty accrual. Our overall accrual is based on our historical experience and our expectation of future conditions, taking into consideration the location and type of customer and the type of laser, which directly correlate to the materials and components under warranty, the duration of the warranty period, and the logistical costs to service the warranty. Additional factors that may impact our warranty accrual include changes in the quality of materials, leadership and training of the production and services departments, knowledge of the lasers and workmanship, training of customers, and adherence to the warranty policies. Additionally, an increase in warranty claims or in the costs associated with servicing those claims would likely result in an increase in the accrual and a decrease in gross profit. We offer extended warranties on certain imaging products. However, all imaging products are initially covered by the manufacturer's warranties.

Litigation and Other Contingencies. We regularly evaluate our exposure to threatened or pending litigation and other business contingencies. Because of the uncertainties related to the amount of loss from litigation and other business contingencies, the recording of losses relating to such exposures requires significant judgment about the potential range of outcomes. As additional information about current or future litigation or other contingencies becomes available, we assess whether such information warrants the recording of expense relating to contingencies. To be recorded as expense, a loss contingency must be both probable and reasonably estimable. If a loss contingency is significant but is not both probable and estimable, we disclose the matter in the *Notes to the Consolidated Financial Statements*.

Income Taxes. Based upon our operating losses during 2017, 2016, and 2015 and the available evidence, management has determined that it is more likely than not that the deferred tax assets as of December 31, 2017 will not be realized in the near term. Consequently, we have established a valuation allowance against our net deferred tax asset totaling approximately \$40.8 million and \$54.3 million as of December 31, 2017 and 2016, respectively. In this determination, we considered factors such as our earnings history, future projected earnings, and tax planning strategies. If sufficient evidence of our ability to generate sufficient future taxable income tax benefits becomes apparent, we may reduce our valuation allowance, resulting in tax benefits in our statement of operations and in additional paid-in-capital. Management evaluates the potential realization of our deferred tax assets and assesses the need for reducing the valuation allowance periodically.

Fair Value of Financial Instruments

Our financial instruments, consisting of cash and cash equivalents, accounts receivable, accounts payable, capital lease obligations and accrued liabilities, approximate fair value because of the liquid or short-term nature of these items.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the principal market (or, if none exists, the most advantageous market) for the specific asset or liability at the measurement date (referred to as the "exit price"). The fair value is based on assumptions that market participants would use, including a consideration of non-performance risk. Under the accounting guidance for value hierarchy, there are three levels of measurement inputs. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are observable, either directly or indirectly. Level 3 inputs are unobservable due to little or no corroborating market data.

Convertible Preferred Stock and Warrant Transactions

On April 18, 2017, the Company completed a private placement with several institutional and individual investors, and certain of its directors and officers, under which the Company sold an aggregate of 80,644 shares of our preferred stock and warrants to purchase up to an aggregate of 3,925,871 unregistered shares of our common stock at an exercise price of \$1.80 per share. Each share of preferred stock was automatically upon receipt of stockholder approval convertible into 100 shares of common stock, reflecting a conversion price equal to \$1.24 per share, which was the closing price of the common stock quoted on the NASDAQ Capital Market on April 10, 2017. On June 30, 2017, we held a meeting of our stockholders and received requisite stockholder approval with respect to the issuance of 8,064,400 shares of common stock upon automatic conversion of the preferred stock and the issuance of our common stock related to exercise of the warrants by certain holders whose warrants were subject to a beneficial ownership limitation. Gross proceeds from the sale were approximately \$10.5 million, and net proceeds, after offering expenses of approximately \$0.3 million, were approximately \$10.2 million. The warrants became exercisable on October 18, 2017, six months after the closing of the private placement, and have a term of five years from the date of issuance. We are using the proceeds of the sale for working capital and general corporate purposes. In connection with the registration rights granted to these investors, we filed a registration statement on Form S-3 with the SEC, which was declared effective on August 24, 2017. In accordance with applicable accounting standards, the \$10.5 million gross proceeds from sale were allocated to the convertible preferred stock and warrants in the amount of \$8.2 million and \$2.3 million, respectively. The allocation was based on the relative fair values of the underlying common stock and warrants as of the commitment date, with the fair value of the warrants determined using a Black Scholes model. This transaction resulted in a discount from allocation of proceeds to separable instruments of \$2.0 million and a beneficial conversion to common stock with a value of \$2.0 million, which has been reflected as a deemed distribution to preferred shareholders in the year ended December 31, 2017.

On August 8, 2016, the Company completed a private placement with several institutional and individual investors, and certain of its directors and officers, under which the Company sold an aggregate of 88,494 shares of our preferred stock and warrants to purchase up to an aggregate of 2,035,398 unregistered shares of our common stock at an exercise price of \$2.00 per share. Each share of preferred stock was automatically upon receipt of stockholder approval convertible into 100 shares of common stock, reflecting a conversion price equal to \$1.13 per share, which was the closing price of the common stock quoted on the NASDAQ Capital Market on July 29, 2016. On September 30, 2016, we held a meeting of our stockholders and received requisite stockholder approval with respect to the issuance of 8,849,400 shares of common stock upon automatic conversion of the preferred stock and the issuance of our common stock related to exercise of the warrants by certain holders whose warrants were subject to a beneficial ownership limitation. Gross proceeds from the sale were approximately \$10.0 million, and net proceeds, after offering expenses of approximately \$0.5 million, were approximately \$9.5 million. The warrants became exercisable on February 8, 2017, six months after the closing of the private placement, and have a term of five years from the date of issuance. We are using the proceeds of the sale for working capital and general corporate purposes. In connection with the registration rights granted to these investors, we filed a registration statement on Form S-3 with the SEC, which was declared effective on November 3, 2016. In accordance with applicable accounting standards, the \$10.0 million gross proceeds from sale were allocated to the convertible preferred stock and warrants in the amount of \$8.9 million and \$1.1 million, respectively. The allocation was based on the relative fair values of the underlying common stock and warrants as of the commitment date, with the fair value of the warrants determined using a Black Scholes model. This transaction resulted in a discount from allocation of proceeds to separable instruments of \$1.1 million and a beneficial conversion to common stock with a value of \$1.1 million, which has been reflected as a deemed distribution to preferred shareholders in the year ended December 31, 2016.

Results of Operations

The following table sets forth certain data from our operating results for each of the years ended December 31, 2017, 2016, and 2015, expressed as percentages of revenue:

	Years Ended December 31,		
	2017	2016	2015
Products and services	99.7 %	99.7 %	99.6 %
License fees and royalty	0.3	0.3	0.4
Net revenue	100.0	100.0	100.0
Cost of revenue	67.8	60.8	67.1
Gross profit	32.2	39.2	32.9
Operating expenses:			
Sales and marketing	35.6	32.8	38.6
General and administrative	20.7	20.2	21.2
Engineering and development	13.3	15.1	15.0
Disposal of internally developed software	1.1	—	—
Excise tax	—	—	0.7
Patent infringement legal settlement	—	—	(1.5)
Total operating expenses	70.7	68.1	74.0
Loss from operations	(38.5)	(28.9)	(41.1)
Non-operating loss, net	1.3	(0.5)	(0.4)
Loss before income taxes	(37.2)	(29.4)	(41.5)
Income tax (benefit) provision	(1.2)	0.3	0.4
Net loss	(36.0)%	(29.7)%	(41.9)%

The following table summarizes our net revenues by category for the years ended December 31, 2017, 2016, and 2015 (dollars in thousands):

	Years Ended December 31,					
	2017		2016		2015	
Laser systems	\$ 29,121	62.0 %	\$ 35,150	67.9 %	\$ 32,691	67.5 %
Imaging systems	3,685	7.9 %	3,066	5.9 %	2,237	4.6 %
Consumables and other	7,332	15.6 %	6,906	13.3 %	6,877	14.2 %
Services	6,660	14.2 %	6,539	12.6 %	6,465	13.3 %
Total products and services	46,798	99.7 %	51,661	99.7 %	48,270	99.6 %
License fees and royalty	128	0.3 %	149	0.3 %	205	0.4 %
Net revenue	\$ 46,926	100.0 %	\$ 51,810	100.0 %	\$ 48,475	100.0 %

Non-GAAP Disclosure

In addition to the financial information prepared in conformity with GAAP, we provide certain historical non-GAAP financial information. Management believes that these non-GAAP financial measures assist investors in making comparisons of period-to-period operating results and that, in some respects, these non-GAAP financial measures are more indicative of the Company's ongoing core operating performance than their GAAP equivalents.

Management believes that the presentation of this non-GAAP financial information provides investors with greater transparency and facilitates comparison of operating results across a broad spectrum of companies with varying capital structures, compensation strategies, derivative instruments, and amortization methods, which provides a more complete understanding of our financial performance, competitive position, and prospects for the future. However, the non-GAAP financial measures presented in this Form 10-K have certain limitations in that they do not reflect all of the costs associated with the operations of our business as determined in accordance with GAAP. Therefore, investors should consider non-GAAP financial measures in addition to, and not as a substitute for, or as superior to, measures of financial performance prepared in accordance with GAAP. Further, the non-GAAP financial measures presented by the Company may be different from similarly named non-GAAP financial measures used by other companies.

Non-GAAP Net Loss. Management uses non-GAAP net loss (defined as net loss before interest, taxes, depreciation and amortization, stock-based compensation, and other non-cash compensation) in its evaluation of the Company's core results of operations and trends between fiscal periods and believes that these measures are important components of its internal performance measurement process. Management believes that this non-GAAP financial information reflects an additional way of viewing aspects of our business that, when viewed with our GAAP results, provides a more complete understanding of factors and trends affecting our business.

Non-GAAP net loss for the periods presented is as follows (in thousands):

	Years Ended December 31,		
	2017	2016	2015
GAAP net loss attributable to common stockholders	\$ (20,829)	\$ (17,555)	\$ (20,278)
Deemed dividend on convertible preferred stock	3,978	2,184	—
GAAP net loss	\$ (16,851)	\$ (15,371)	\$ (20,278)
Adjustments:			
Interest income, net	(42)	(74)	(74)
Income tax (benefit) provision	(582)	151	178
Depreciation and amortization	1,203	1,048	880
Disposal of internally developed software	505	—	—
Stock-based and other non-cash compensation	2,207	3,065	3,350
Non-GAAP net loss	\$ (13,560)	\$ (11,181)	\$ (15,944)

Comparison of Results of Operations

Year Ended December 31, 2017 Compared with Year Ended December 31, 2016

Net Revenue. Net revenue for the year ended December 31, 2017 ("Fiscal 2017") was \$46.9 million, a decrease of \$4.9 million, or 9%, as compared with net revenue of \$51.8 million for the year ended December 31, 2016 ("Fiscal 2016"). Domestic revenues were \$29.3 million, or 62% of net revenue, for Fiscal 2017 compared to \$33.4 million, or 64% of net revenue, for Fiscal 2016. International revenues for Fiscal 2017 were \$17.6 million, or 38% of net revenue, compared to \$18.4 million, or 36% of net revenue for Fiscal 2016.

The decrease in year-over-year net revenue resulted from decreases in worldwide laser system revenue, international imaging systems revenue, international consumables and other revenue, international services revenue and domestic license and royalties revenue, partially offset by increases in domestic imaging systems revenue, domestic consumables and other revenue and domestic services revenue. Our goal has been to refocus on strengthening our leadership position in dental markets worldwide through increased focus on our professional customers and their patients. We have strengthened our management team with new key personnel and invested in our sales resources both domestically and internationally.

Laser system net revenues decreased by approximately \$6.0 million, or 17%, in Fiscal 2017 compared to Fiscal 2016. The laser systems revenue decrease was driven by a 28% decline in domestic revenue and a 3% decline in international revenue.

Imaging system net revenue increased by approximately \$0.6 million, or 20%, in Fiscal 2017 compared to Fiscal 2016. This increase was due to increased overall market interest in intra-oral scanning devices, and our favorable positioning as a distributor.

Consumables and other net revenue, which includes products such as disposable tips and shipping revenue, increased approximately \$0.4 million, or 6%, in Fiscal 2017, as compared to Fiscal 2016. The increase in consumables and other net revenue was primarily a result of auxiliary sales to our growing laser customer base.

License fees and royalty revenue decreased by 14%, to approximately \$0.1 million in Fiscal 2017 compared to Fiscal 2016. License fees and royalty revenues are associated with intellectual property related to our laser technologies. The decrease was primarily due to the settlement of the Fotona Proizvodnja Optoelektronskih Naprav D.D. and Fotona LLC intellectual property litigation (the "Fotona Litigation") from Fiscal 2015. We anticipate license fees and royalty revenue to be consistent with Fiscal 2017 for the year ending December 31, 2018 ("Fiscal 2018").

Cost of Revenue. Cost of revenue in Fiscal 2017 increased by \$0.3 million, or 1%, to \$31.8 million, or 68% of net revenue, compared with cost of revenue of \$31.5 million, or 61% of net revenue, in Fiscal 2016.

Gross Profit. Gross profit as a percentage of revenue typically fluctuates with product and regional mix, selling prices, product costs and revenue levels. Gross profit for Fiscal 2017 was \$15.1 million, or 32% of net revenue, a decrease of approximately \$5.2 million, or 26%, as compared with gross profit of \$20.3 million, or 39% of net revenue, for Fiscal 2016. The decrease in gross profit was mainly attributable to promotional introductory pricing of Waterlase Express, unabsorbed fixed costs due to lower revenue, and an increase in imaging revenue, which has lower product distribution margins than laser systems revenue.

Operating Expenses. Operating expenses for Fiscal 2017 were \$33.2 million, or 71% of net revenue, a decrease of approximately \$2.1 million, or 6%, as compared with \$35.3 million, or 68% of net revenue, for Fiscal 2016. The year-over-year decrease in expense is primarily due to a \$0.7 million decrease in commissions expenses and \$0.8 million decrease in stock-based compensation expenses. See the following expense categories for further explanations. We expect that operating expenses as a percentage of net revenue for Fiscal 2018 to decrease from Fiscal 2017.

Sales and Marketing Expense. Sales and marketing expenses for Fiscal 2017 decreased by \$0.3 million, or 2%, to \$16.7 million, or 36% of net revenue, as compared with \$17.0 million, or 33% of net revenue, during Fiscal 2016. The decrease was primarily a result of decreased commissions of \$0.7 million, partially offset by increased payroll and consulting-related expenses of \$0.1 million, increased convention-related expenses of \$0.1 million and increased travel and travel-related expenses of \$0.2 million. The decrease in commissions was driven by decreased sales in Fiscal 2017 compared to Fiscal 2016. The increase in payroll and consulting-related expenses resulted primarily from increased incentive compensation of \$0.3 million, partially offset by a decrease of \$0.2 million in stock-based compensation due to fewer grants. In the first quarter of 2017, we participated in the International Dental Show in Cologne, Germany, which led to higher convention-related expenses and travel expenditures. As we continue efforts to transform and drive to revenue growth, we expect sales and marketing expenses to decrease as a percentage of revenue in Fiscal 2018.

General and Administrative Expense. General and administrative expenses for Fiscal 2017 decreased by \$0.7 million, or 7%, to \$9.7 million, or 21% of net revenue, as compared with \$10.5 million, or 20% of net revenue, for Fiscal 2016. The overall decrease to general and administrative expenses was primarily due to decreased payroll and consulting-related expenses of \$0.8 million, and decreased patent and legal expenses of \$0.3 million, partially offset by increased provision for doubtful accounts of \$0.2 million and increased bank fees of \$0.1 million. The decreased payroll and consulting-related expenses resulted primarily from decreased recruiting fees of \$0.3 million and decreased stock-based compensation expense of \$0.6 million due to the reassessment of certain performance based equity awards, partially offset by an increase in salaries and wages of \$0.1 million. The decrease in patent and legal expenses resulted from a decrease in legal and litigation fees in the normal course of business of \$0.3 million. We expect general and administrative expenses to decrease as a percentage of revenue in Fiscal 2018.

Engineering and Development Expense. Engineering and development expenses for Fiscal 2017 decreased by \$1.6 million, or 20%, to \$6.3 million, or 13% of net revenue, as compared with \$7.8 million, or 15% of net revenue, in Fiscal 2016. The decrease was primarily related to decreased payroll, consulting and temporary labor expenses of \$0.9 million and decreased supplies expenses of \$0.8 million. The decrease in payroll, consulting and temporary labor expenses resulted primarily from decreased consulting fees of \$0.9 million. The decrease in supplies expenses resulted primarily from decreased operating supplies of \$0.6 million. We expect to continue our investment in engineering and development activity, although we expect engineering and development expenses to a decrease as a percentage of revenue in Fiscal 2018.

Disposal of Internally Developed Software Expense. Disposal of internally developed software expense for Fiscal 2017 was \$0.5 million. In 2013, we began our program to deploy a new global enterprise resource planning (“ERP”) system developed by SAP. After careful evaluation, we have concluded that this new ERP system does not fit into our current business model. Accordingly, we have stopped our global ERP deployment and disposed of all related assets.

Non-Operating Income (Loss)

Gain (Loss) on Foreign Currency Transactions. We recognized a \$0.6 million gain on foreign currency transactions for Fiscal 2017 compared to a \$0.3 million loss for Fiscal 2016, due to exchange rate fluctuations primarily between the U.S. dollar and the Euro.

Interest Income (Expense), Net. Interest income during Fiscal 2017 represented interest recognized from the discounted present value of the settlement in connection with the Fotona Litigation. Interest expense in Fiscal 2017 consisted of interest incurred on our capital lease obligations in connection with the lease of information technology equipment. Interest income, net comprised of approximately 0.1% of net revenue, for Fiscal 2017, which is consistent with interest income of 0.1% of net revenue for Fiscal 2016.

(Benefit) Provision for Income Taxes. Our benefit for income taxes was \$0.6 million for Fiscal 2017, a change of \$0.7 million, as compared with our provision of income taxes of \$0.2 million in Fiscal 2016. The change is due to the Tax Cuts and Jobs Act of 2017, which decreased the corporate tax rate from 34% to 21%.

Net Loss. For the reasons stated above, our net loss was \$16.9 million for Fiscal 2017 compared to a net loss of \$15.4 million for Fiscal 2016. The increase in net loss of approximately \$1.5 million, or 10%, was primarily due to increased loss from operations of \$3.1 million, including a non-cash expense related to the disposal of internally developed software of \$0.5 million due to the decision to cancel future deployments of a new ERP system, partially offset by increased gain of foreign currency transactions of \$0.9 million and a change in income tax benefit, net of \$0.7 million.

Year Ended December 31, 2016 Compared with Year Ended December 31, 2015

Net Revenue. Net revenue for Fiscal 2016 was \$51.8 million, an increase of \$3.3 million, or 7%, as compared with net revenue of \$48.5 million for the year ended December 31, 2015 ("Fiscal 2015"). Domestic revenues were \$33.4 million, or 64% of net revenue, for Fiscal 2016 compared to \$29.5 million, or 61% of net revenue, for Fiscal 2015. International revenues for Fiscal 2016 were \$18.4 million, or 36% of net revenue, compared to \$19.0 million, or 39% of net revenue for Fiscal 2015. The increase in period-over-period net revenue resulted from increases in domestic laser system revenue, imaging systems revenue, consumables and other revenue, and services revenue, partially offset by decreases in international laser systems revenue, imaging systems revenue, consumables and other revenue, services revenue, and domestic license and royalties revenue.

Laser system net revenues increased by approximately \$2.5 million, or 8%, in Fiscal 2016 compared to Fiscal 2015. We experienced an improvement in the sales of our core laser products during Fiscal 2016 as compared with the prior year. In 2016, we continued to realize some of the changes to our sales cycle that were implemented late in 2015.

Imaging system net revenue increased by approximately \$0.8 million, or 37%, in Fiscal 2016 compared to Fiscal 2015. This increase was due to increased market overall interest in intra-oral scanning devices, and our favorable positioning as a distributor.

Consumables and other net revenue, which includes products such as disposable tips and shipping revenue, increased approximately 0.4% in Fiscal 2016, as compared to Fiscal 2015. The slight increase in consumables and other net revenue was primarily a result of auxiliary sales to our growing laser customer base.

License fees and royalty revenue decreased by approximately \$0.1 million, or 27%, to approximately \$0.1 million in Fiscal 2016 compared to \$0.2 million in Fiscal 2015. License fees and royalty revenues are associated with intellectual property related to our laser technologies. The decrease was primarily due to the settlement of the Fotona Litigation from Fiscal 2015.

Cost of Revenue. Cost of revenue in Fiscal 2016 decreased by \$1.0 million, or 3%, to \$31.5 million, or 61% of net revenue, compared with cost of revenue of \$32.5 million, or 67% of net revenue, in Fiscal 2015. The decrease in cost of revenue was mainly attributable to the increased concentration of domestic sales that typically have higher margins than our international sales and reduced warranty expenses from quality improvements.

Gross Profit. Gross profit as a percentage of revenue typically fluctuates with product and regional mix, selling prices, product costs and revenue levels. Gross profit for Fiscal 2016 was \$20.3 million, or 39% of net revenue, an increase of approximately \$4.3 million, or 27%, as compared with gross profit of \$16.0 million, or 33% of net revenue, for Fiscal 2015. Improvements in gross profit reflect a larger concentration of domestic laser sales, specifically the Waterlase iPlus, which typically have higher product margins than our international sales due to higher pricing.

Operating Expenses. Operating expenses for Fiscal 2016 were \$35.3 million, or 68% of net revenue, a decrease of approximately \$0.6 million or 2%, as compared with \$35.9 million, or 74% of net revenue, for Fiscal 2015. The year-over-year decrease in expenses is primarily due to a \$1.1 million decrease in payroll-related expenses. See the following expense categories for further explanations.

Sales and Marketing Expense. Sales and marketing expenses for Fiscal 2016 decreased by \$1.7 million, or 9%, to \$17.0 million, or 33% of net revenue, as compared with \$18.7 million, or 39% of net revenue, during Fiscal 2015. The decrease was primarily a result of decreased payroll and consulting-related expenses of \$0.9 million, decreased media and advertising expenses of \$0.6 million, decreased supplies of \$0.2 million, and decreased commissions of \$0.2 million. The decrease in payroll and consulting-related expenses resulted primarily from decreased salary expenses of \$0.3 million, a decrease of \$0.2 million in stock-based compensation due to fewer grants to existing and new employees, a decrease of \$0.2 million in consulting expenses, and a decrease of \$0.1 million in severance-related expenses associated with our internal corporate organizational restructuring changes in the second half of 2015. The decrease in media and advertising expenses resulted primarily from decreased advertising expenses of \$0.6 million and decreased public relations materials expenses of \$0.2 million, partially offset by increased product literature expenses of \$0.1 million.

General and Administrative Expense. General and administrative expenses for Fiscal 2016 increased by \$0.2 million, or 2%, to \$10.5 million, or 20% of net revenue, as compared with \$10.3 million, or 21% of net revenue, for Fiscal 2015. The overall increase to general and administrative expenses was primarily due to increased patent and legal expenses of \$1.5 million, partially offset by decreased payroll and consulting-related expenses of \$0.6 million, decreased state and local taxes, licenses and fees of \$0.3 million, decreased investor relations expenses of \$0.2 million, and a decrease to our provision for doubtful accounts of \$0.3 million. The Fiscal 2016 increase in legal expenses resulted from a \$1.7 million reduction in legal fees pertaining to the positive settlement outcome of the 2014 shareholder litigation matter recognized during the fourth quarter of 2015. The decrease in payroll-related and consulting-related expenses resulted primarily from a decrease in severance expenses of \$0.3 million related to the change in Chief Executive Officer in 2015.

Engineering and Development Expense. Engineering and development expenses for Fiscal 2016 increased by \$0.5 million, or 7%, to \$7.8 million, or 15% of net revenue, as compared with \$7.3 million, or 15% of net revenue, in Fiscal 2015. The increase was primarily related to increased payroll, consulting and temporary labor expenses of \$0.4 million.

Excise Tax Expense. Beginning in 2013, the Affordable Care Act imposed a 2.3% medical device excise tax on certain product sales to customers located in the U.S. Excise tax expenses for Fiscal 2016 was \$0, or 0% of net revenue, as compared with \$0.4 million, or 1% of net revenue, for Fiscal 2015. The decrease of \$0.4 million, or 100%, was directly associated with the Protecting Americans from Tax Hikes Act of 2015, which suspended the medical device excise tax for calendar years 2016 and 2017.

Non-Operating Income (Loss)

(Loss) Gain on Foreign Currency Transactions. We recognized a \$0.3 million loss on foreign currency transactions for Fiscal 2016 compared to a \$0.3 million loss for Fiscal 2015 due to exchange rate fluctuations primarily between the U.S. dollar and the Euro. During Fiscal 2016, the Euro continued to fluctuate against the U.S. dollar.

Interest Income (Expense), Net. Interest income during Fiscal 2016 represented interest recognized from the discounted present value of the settlement in connection with the Fotona Litigation. Interest expense in Fiscal 2016 consisted of interest incurred on our capital lease obligations in connection with the lease of information technology equipment. Interest income, net totaled approximately \$0.1 million of interest income, or 0.1% of net revenue, for Fiscal 2016, which is consistent with interest income of \$0.1 million, or 0.1% of net revenue for Fiscal 2015.

Provision (benefit) for Income Taxes. Our provision for income taxes was \$0.2 million for Fiscal 2016, a decrease of 15%, as compared with our provision of income taxes of \$0.2 million in Fiscal 2015. The decrease is due to a decrease in income earned in foreign jurisdictions during Fiscal 2016 and state income tax.

Net Loss. For the reasons stated above, our net loss was \$15.4 million for Fiscal 2016 compared to a net loss of \$20.3 million for Fiscal 2015. The decrease in net loss of approximately \$4.9 million, or 24%, was primarily due to increased gross profit of \$4.4 million and decreased operating expenses of \$0.6 million.

Liquidity and Capital Resources

At December 31, 2017, we had approximately \$11.9 million in cash and cash equivalents, including restricted cash equivalents. Management defines cash and cash equivalents as highly liquid deposits with original maturities of 90 days or less when purchased. The increase in our cash and cash equivalents by \$2.7 million from December 31, 2016 was primarily due to cash provided by financing activities of \$21.6 million, partially offset by cash used in operating and investing activities of \$18.4 million and \$0.7 million, respectively, and the effect of exchange rates on cash of \$0.3 million. The \$18.4 million of net cash used in operating activities was primarily driven by the Company's net loss of \$16.9 million during the year.

At December 31, 2017, we had approximately \$22.7 million in working capital. Our principal sources of liquidity at December 31, 2017, consisted of approximately \$11.9 million in cash, cash equivalents and restricted cash and \$10.1 million of net accounts receivable.

We have reported recurring losses from operations and have not generated cash from operations for the three years ended December 31, 2017. Our level of cash used in operations, the potential need for additional capital, and the uncertainties surrounding our ability to raise additional capital, raise substantial doubt about our ability to continue as a going concern. The accompanying financial statements have been prepared on a going concern basis, which assumes that we will continue in operation for the next 12 months and will be able to realize our assets and discharge our liabilities and commitments in the normal course of business. The financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

In order for us to continue operations beyond the next 12 months and be able to discharge our liabilities and commitments in the normal course of business, we must sell our products directly to end users and through distributors, establish profitable operations through increased sales, decrease expenses, generate cash from operations, or obtain additional funds when needed. We intend to improve our financial condition and ultimately improve our financial results by increasing revenues through expansion of our product offerings, continuing to expand and develop our field sales force and distributor relationships both domestically and internationally, forming strategic arrangements within the dental and medical industries, educating dental and medical patients as to the benefits of our advanced medical technologies, and reducing expenses.

On March 6, 2018, BIOLASE and two of its wholly-owned subsidiaries (such subsidiaries, together with BIOLASE, the “Borrower”) entered into a Business Financing Agreement (the “Business Financing Agreement”). Pursuant to the terms and conditions of the Business Financing Agreement, Western Alliance has agreed to provide the Borrower a secured revolving line of credit permitting the Borrower to borrow or receive letters of credit up to the lesser of \$6.0 million (subject to a \$6.0 million credit limit relating to domestic eligible accounts receivable (the “domestic credit limit”) and a \$3.0 million credit limit relating to export-related eligible accounts receivable (the “EXIM credit limit”)) and the borrowing base, which is defined as the sum of the domestic borrowing base (up to 75.0% of the Borrower’s eligible domestic accounts receivable less such reserves as Western Alliance may deem proper and necessary) and the export-related borrowing base (up to 85.0% of the Borrower’s eligible export-related accounts receivable less such reserves as Western Alliance may deem proper and necessary). The Business Financing Agreement expires on March 6, 2020, and the Borrower’s obligations thereunder are secured by a security interest in all of the Borrower’s assets.

Amounts outstanding under the Business Financing Agreement bear interest at a per annum floating rate equal to the greater of 4.5% or the “Prime Rate” published in the Money Rates section of the Western Edition of The Wall Street Journal (or such other rate of interest publicly announced from time to time by Western Alliance as its “Prime Rate”), plus 1.5% with respect to advances made under the line of credit, plus an additional 5.0% during any period that an event of default has occurred and is continuing. The commitment fee under the Business Financing Agreement is 0.25% of the domestic credit limit and 1.75% of the EXIM credit limit and is payable on March 6, 2018 and each anniversary thereof.

Additional capital requirements may depend on many factors, including, among other things, the rate at which our business grows, demands for working capital, manufacturing capacity, and any acquisitions that we may pursue. From time to time, we could be required, or may otherwise attempt, to raise capital through either equity or debt offerings. We cannot provide assurance that we will enter into any such equity or debt financings in the future or that the required capital will be available on acceptable terms, if at all, or that any such financing activity will not be dilutive to our stockholders.

Concentration of Credit Risk

Financial instruments, which potentially expose us to a concentration of credit risk, consist principally of cash and cash equivalents, restricted cash, and trade accounts receivable. We maintain our cash and cash equivalents and restricted cash with established commercial banks. At times, balances may exceed federally insured limits. To minimize the risk associated with trade accounts receivable, we perform ongoing credit evaluations of customers’ financial condition and maintain relationships with our customers that allow us to monitor changes in business operations so we can respond as needed. We do not, generally, require customers to provide collateral before we sell them our products. However we have required certain distributors to make prepayments for significant purchases of our products.

Receivables and Allowance for Doubtful Accounts

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in the existing accounts receivable. We determine the allowance based on a quarterly specific account review of past due balances. All other balances are reviewed on a pooled basis by age of receivable. Account balances are charged off against the allowance when it is probable the receivable will not be recovered. We do not have any off-balance-sheet credit exposure related to our customers.

Consolidated Cash Flows

The following table summarizes our statements of cash flows for Fiscal 2017, Fiscal 2016, and Fiscal 2015 (in thousands):

	Years Ended December 31,		
	2017	2016	2015
Net cash (used in) provided by:			
Operating activities	\$ (18,412)	\$ (10,647)	\$ (17,772)
Investing activities	(747)	(1,414)	(1,778)
Financing activities	21,618	9,350	(105)
Effect of exchange rates on cash	262	(64)	(206)
Net change in cash and cash equivalents	<u>\$ 2,721</u>	<u>\$ (2,775)</u>	<u>\$ (19,861)</u>

Fiscal 2017 Compared to Fiscal 2016

The \$7.8 million increase in net cash used in operating activities for Fiscal 2017 compared to Fiscal 2016 was primarily due to an increase in our net loss of \$1.5 million, decreased stock-based compensation of \$0.9 million and decreased accounts payable and accrued liabilities of \$5.0 million. The increased net loss was primarily driven by an increase in loss from operations of \$3.1 million, partially offset by a non-operating gain (loss), net of \$0.9 million a change in income tax benefit, net of \$0.7 million. Cash used in operating activities for Fiscal 2017 totaled \$18.4 million and was primarily comprised of net loss of \$16.9 million, adjustments to reconcile net loss to net cash and cash equivalents of \$3.8 million and cash outflow from net changes in assets and liabilities of \$5.4 million. The \$5.4 million net decrease in our operating assets and liabilities was primarily due to a decrease in accounts payable and accrued liabilities of \$5.0 million related to the timing of our payments.

Cash used in investing activities for Fiscal 2017 totaled \$0.7 million compared to \$1.4 million for Fiscal 2016. The \$0.7 million decrease in net cash used in investing activities was due to a \$0.7 million decrease in capital expenditures during Fiscal 2017 compared to Fiscal 2016. The period-over-period decrease was primarily due to capital expenditures for the implementation of a new enterprise resource planning system, which has been put on hold in 2017. We expect capital expenditures to total approximately \$0.6 million in Fiscal 2018, and we expect depreciation and amortization to total approximately \$1.3 million for Fiscal 2018.

The \$21.6 million increase in net cash provided by financing activities for Fiscal 2017 compared to Fiscal 2016 was primarily due to net proceeds from our rights offering in December 2017 and our equity offering in April 2017 totaling \$21.6 million. See Note 7 to the *Notes to the Consolidated Financial Statements — Stockholders' Equity* for more information.

The \$0.3 million effect of exchange rate on cash for Fiscal 2017 was due to a recognized gain on foreign currency transactions, primarily the Euro currency conversion rates during 2017.

Fiscal 2016 Compared to Fiscal 2015

The \$7.1 million decrease in net cash used in operating activities for Fiscal 2016 compared to Fiscal 2015 was primarily due to our decreased net loss of \$4.9 million. The decreased net loss was primarily driven by an increase in gross profit of \$4.4 million. Cash used in operating activities for Fiscal 2016 totaled \$10.7 million and was primarily comprised of net loss of \$15.4 million, adjustments to reconcile net loss to net cash and cash equivalents of \$4.3 million and net changes in assets and liabilities of \$0.5 million.

Cash used in investing activities for Fiscal 2016 totaled \$1.4 million compared to \$1.8 million for Fiscal 2015. The \$0.4 million decrease in net cash used in investing activities was primarily due to a \$0.4 million decrease in capital expenditures during Fiscal 2016 compared to Fiscal 2015 as a result of the 2015 buildout of our world-class training facility. Fiscal 2016 cash used in investing activities relate to the continued conversion of a new enterprise resource planning software.

The \$9.5 million increase in net cash provided by financing activities for Fiscal 2016 compared to Fiscal 2015 was primarily due to net proceeds from our equity offering in August 2016 totaling \$9.5 million. See Note 7 to the *Notes to the Consolidated Financial Statements — Stockholders' Equity* for more information.

The \$0.1 million increase in effect of exchange rates on cash for Fiscal 2016 compared to Fiscal 2015 was primarily due to \$332,000 loss on foreign currency transactions.

Contractual Obligations

We lease our primary facility under a non-cancellable operating lease that expires in April 2020.

In February 2015, the Company entered into a 30-month capital lease agreement for information technology equipment. In February 2018, the Company extended the agreement for information technology equipment for an additional lease term of 18 months. In accordance with relevant accounting guidance, the renewal of this lease constituted a new lease and is classified by the Company as an operating lease.

The following table presents our expected cash requirements for contractual obligations outstanding as of December 31, 2017, for the years ending as indicated below (in thousands):

	Less Than 1 Year	1 to 3 Years	3 to 5 Years	More Than 5 years	Total
Operating lease obligations	\$ 814	\$ 1,039	\$ —	\$ —	\$ 1,853
Purchase obligations	10,278	633	—	—	10,911
Total	<u>\$ 11,092</u>	<u>\$ 1,672</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 12,764</u>

Purchase obligations relate to purchase orders with suppliers that we expect to complete primarily during the year ending December 31, 2018. In conformity with GAAP, purchase obligations and operating lease obligations are not reported in the consolidated balance sheet as of December 31, 2017.

Recent Accounting Pronouncements

See Note 2 to the *Notes to the Consolidated Financial Statements — Summary of Significant Accounting Policies — Recent Accounting Pronouncements* to the Consolidated Financial Statements in Part IV, Item 15 of this Annual Report on Form 10-K, which is incorporated herein by reference.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements as defined in Regulation S-K Item 303(A)(4)(ii).

Item 8. Financial Statements

All financial statements required by this Item 8, including the report of the independent registered public accounting firm, are listed in Part IV, Item 15 of this Form 10-K, are set forth beginning on Page F-1 of this Form 10-K, and are hereby incorporated herein by reference.

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

None.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

Our management has evaluated, with the participation of our President and Chief Executive Officer and Chief Financial Officer, the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on that evaluation, our President and Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2017.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework established by the Committee of Sponsoring Organizations of the Treadway Commission entitled "Internal Control — Integrated Framework (2013)" (the "COSO Framework"). Based on our evaluation under the COSO Framework, our management concluded that our internal control over financial reporting was effective as of December 31, 2017. Our internal control over financial reporting was not subject to attestation by our independent registered public accounting firm, as we are a smaller reporting company.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting that occurred during the Company's fiscal quarter ended December 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Information regarding our executive officers is included in Part I of this Form 10-K under "Item 1. Business — Executive Officers of the Registrant." In addition, the information set forth under the caption "Election of Directors" and "Security Ownership of Certain Beneficial Owners and Management — Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement is incorporated by reference herein.

The Biolase, Inc. Code of Business Conduct and Ethics applies to all of our employees, officers, and directors, including our President and Chief Executive Officer. The Code of Business Conduct can be found on our website at the following address: http://media.corporate-ir.net/media_files/nsd/blti/corpgov/CodeofConductandEthics.pdf.

Item 11. Executive Compensation

The information set forth under the captions "Executive Compensation" and "Director Compensation" in the Proxy Statement is incorporated by reference herein.

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

The information set forth under the caption "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement and the information set forth under the caption "Equity Compensation Plan Information" in Item 5 of this Form 10-K are incorporated by reference herein.

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

The information set forth under the captions "Election of Directors" and "Certain Relationships and Related Transactions" in the Proxy Statement is incorporated by reference herein.

Item 14. Principal Accountant Fees and Services

The information set forth under the caption "Principal Accountant Fees and Services" in the Proxy Statement is incorporated by reference herein.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) The following documents are filed as part of this Annual Report on Form 10-K beginning on the pages referenced below:

(1) *Financial Statements:*

	Page
Report of Independent Registered Public Accounting Firm	F-2
Consolidated Balance Sheets as of December 31, 2017 and 2016	F-3
Consolidated Statements of Operations and Comprehensive Loss for the years ended December 31, 2017, 2016, and 2015	F-4
Consolidated Statements of Stockholders' Equity for the years ended December 31, 2017, 2016, and 2015	F-5
Consolidated Statements of Cash Flows for the years ended December 31, 2017, 2016, and 2015	F-7
Notes to Consolidated Financial Statements	F-8

(2) *Financial Statement Schedule:*

Schedule II— Consolidated Valuation and Qualifying Accounts and Reserves for the years ended December 31, 2017, 2016, and 2015	S-1
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All other schedules have been omitted as they are not applicable, not required or the information is included in the consolidated financial statements or the notes thereto.

(3) *Exhibits:*

The exhibits filed as a part of this Annual Report on Form 10-K are listed in the accompanying Exhibit Index on page 59.

Item 16. Form 10-K Summary

None

BIOLASE, INC.
Index to Exhibits

Exhibit	Description	Filed Herewith	Incorporated by Reference			
			Form	Period Ending/Date of Report	Exhibit	Filing Date
3.1.1	Restated Certificate of Incorporation, including, (i) Certificate of Designations, Preferences and Rights of 6% Redeemable Cumulative Convertible Preferred Stock of the Registrant; (ii) Certificate of Designations, Preferences and Rights of Series A 6% Redeemable Cumulative Convertible Preferred Stock of the Registrant; (iii) Certificate of Correction Filed to Correct a Certain Error in the Certificate of Designation of the Registrant; and (iv) Certificate of Designations of Series B Junior Participating Cumulative Preferred Stock of the Registrant		S-1, Amendment No. 1	12/23/2005	3.1	12/23/2005
3.1.2	Amendment to Restated Certificate of Incorporation		8-K	05/10/2012	3.1	05/16/2012
3.1.3	Second Amendment to Restated Certificate of Incorporation		8-A/A	11/04/2014	3.1.3	11/04/2014
3.1.4	Third Amendment to Restated Certificate of Incorporation		S-3	07/21/2017	3.4	07/21/2017
3.1.5	Certificate of Elimination of Series B Junior Participating Cumulative Preferred Stock		8-K	11/10/2015	3.1	11/12/2015
3.1.6	Certificate of Designations, Preferences and Rights of Series C Participating Convertible Preferred Stock		8-K	08/08/2016	3.1	08/08/2016
3.1.7	Certificate of Elimination of Series C Participating Convertible Preferred Stock		8-K	04/18/2017	3.1	04/20/2017
3.1.8	Certificate of Designations, Preferences and Rights of Series D Participating Convertible Preferred Stock		8-K	04/18/2017	3.2	04/20/2017
3.2	Sixth Amended and Restated Bylaws of the Registrant, adopted on June 26, 2014		8-K	06/26/2014	3.1	06/30/2014
4.1	Form of Warrant issued on November 7, 2014		8-K	11/03/2014	99.1	11/07/2014
4.2	Form of Warrant issued on August 8, 2016		8-K	08/01/2016	99.1	08/02/2016
4.3	Form of Warrant issued on April 18, 2017		DEF14A		D	05/19/2017
4.4	Form of Warrant issued on March 6, 2018	X				
4.5	Standstill Agreement, dated November 10, 2015, by and among the Registrant, Jack W. Schuler, Renate Schuler and the Schuler Family Foundation		8-K	11/10/2015	99.1	11/12/2015
4.6	Standstill Agreement, dated November 10, 2015, by and among the Registrant and Larry N. Feinberg, Oracle Partners, L.P., Oracle Institutional Partners, L.P., Oracle Ten Fund Master, L.P., Oracle Associates, LLC, and Oracle Investment Management, Inc.		8-K	11/10/2015	99.2	11/12/2015

Exhibit	Description	Filed Herewith	Incorporated by Reference			
			Form	Period Ending/Date of Report	Exhibit	Filing Date
4.7	Amendment to Standstill Agreement, dated August 1, 2016, by and among the Registrant, Jack W. Schuler, Renate Schuler and the Schuler Family Foundation		8-K	08/01/2016	99.2	08/02/2016
4.8	Amendment to Standstill Agreement, dated August 1, 2016, by and among the Registrant, Larry N. Feinberg, Oracle Partners, L.P., Oracle Institutional Partners, L.P., Oracle Ten Fund Master, L.P., Oracle Associates, LLC and Oracle Investment Management, Inc.		8-K	08/01/2016	99.3	08/02/2016
4.9	Amendment to Standstill Agreement, dated November 9, 2017, by and among the Registrant, Jack W. Schuler, Renate Schuler and the Schuler Family Foundation		8-K	11/09/2017	99.1	11/09/2017
4.10	Amendment to Standstill Agreement, dated November 9, 2017, by and among the Registrant, Larry N. Feinberg, Oracle Partners, L.P., Oracle Institutional Partners, L.P., Oracle Ten Fund Master, L.P., Oracle Associates, LLC and Oracle Investment Management, Inc.		8-K	11/09/2017	99.2	11/09/2017
10.1*	2002 Stock Incentive Plan, as amended		DEF 14A		A	04/07/2016
10.2*	Form of Stock Option Agreement under the 2002 Stock Incentive Plan		10-K	12/31/2004	10.26	07/19/2005
10.3*	Form of Option Award Notice for California Employees under the 2002 Stock Incentive Plan		10-Q	09/30/2015	10.2	11/06/2015
10.4*	Form of Option Award Notice for Non-California Employees under the 2002 Stock Incentive Plan		10-Q	09/30/2015	10.3	11/06/2015
10.5*	Form of Option Award Notice for Non-Employee Directors under the 2002 Stock Incentive Plan		10-Q	09/30/2015	10.4	11/06/2015
10.6*	Form of Restricted Stock Unit Award Notice for Non-Employee Directors under the 2002 Stock Incentive Plan		10-Q	09/30/2015	10.5	11/06/2015
10.8*	Form of Indemnification Agreement between the Registrant and its officers and directors		10-Q	09/30/2005	10.1	11/09/2005
10.9	Lease, dated January 10, 2006, by and between the Registrant and The Irvine Company LLC		8-K	01/10/2006	10.1	01/17/2006
10.10	Third Amendment to Lease, dated March 16, 2015, by and between the Registrant and The Irvine Company LLC		10-Q	03/31/2015	10.3	05/01/2015
10.11†	Letter Agreement, dated June 28, 2006, by and between the Registrant and The Procter & Gamble Company		10-Q	06/30/2006	10.1	08/09/2006
10.12†	License Agreement, dated January 24, 2007, by and between the Registrant and The Procter & Gamble Company		10-Q	03/31/2007	10.1	05/10/2007

Exhibit	Description	Filed Herewith	Incorporated by Reference			
			Form	Period Ending/Date of Report	Exhibit	Filing Date
10.13	Letter Agreement, dated June 28, 2011, by and between the Registrant and The Proctor & Gamble Company		10-Q	06/30/2011	10.2	08/11/2011
10.14	Securities Purchase Agreement, dated August 1, 2016, among the Registrant and the investors listed on Schedule I thereto		8-K	08/01/2016	99.1	08/02/2016
10.15	Securities Purchase Agreement, dated April 11, 2017, among the Registrant and the investors listed on Schedule I thereto		8-K	04/11/2017	99.1	04/14/2017
10.16*	Employment Agreement, dated February 22, 2015 and entered into on February 24, 2015, by and between the Registrant and David Dreyer		10-K	12/31/2015	10.25	03/06/2015
10.17*	Employment Agreement, dated May 14, 2015, by and between the Registrant and Harold C. Flynn, Jr.		10-Q	06/30/2015	10.2	08/07/2015
10.18*	Inducement Restricted Stock Unit Award Agreement, dated July 14, 2015, by and between the Registrant and Harold C. Flynn, Jr.		8-K	07/12/2015	10.2	07/15/2015
10.19*	Acknowledgment Letter, dated November 22, 2016, by and between the Registrant and Harold C. Flynn, Jr.		10-K	12/31/2016	10.18	03/10/2017
10.20*	Transition Letter Agreement, dated December 28, 2016, by and between the Registrant and David Dreyer		10-K	12/31/2016	10.19	03/10/2017
10.21*	Separation Agreement, dated January 13, 2017, by and between the Registrant and David Dreyer		10-K	12/31/2016	10.20	03/10/2017
10.22*	Employment Agreement, dated February 23, 2017, by and between the Registrant and Mark Nelson		10-K	12/31/2016	10.21	03/10/2017
10.23	Commitment Letter, dated September 26, 2017, between each of Oracle Partners, LP, Oracle Institutional Partners, LP and Oracle Ten Fund Master, LP and the Registrant		S-1	09/29/2017	10.23	09/29/2017
10.24	Commitment Letter, dated September 26, 2017, between each of Renate Schuler, Jack W. Schuler Living Trust and Schuler Family Foundation and the Registrant		S-1	09/29/2017	10.24	09/29/2017
10.25*	Form of Stock Option Agreement for inducement grants made to John R. Beaver on September 30, 2017		8-K	09/30/2017	10.1	10/03/2017
10.26	Business Financing Agreement, dated as of March 6, 2018, by and among the Registrant, Western Alliance Bank, BL Acquisition Corp. and BL Acquisition II Inc.	X				

Exhibit	Description	Filed Herewith	Incorporated by Reference		
			Form	Period Ending/Date of Report	Filing Date
10.27	Export-Import Bank of the United States Working Capital Guarantee Program Borrower Agreement, dated as of March 6, 2018, by and between the Registrant in favor of the Export Import Bank of the United States and Western Alliance Bank	X			
10.28	Export-Import Bank of the United States Working Capital Guarantee Program Borrower Agreement, dated as of March 6, 2018, by and between BL Acquisition Corp. in favor of the Export Import Bank of the United States and Western Alliance Bank	X			
10.29	Export-Import Bank of the United States Working Capital Guarantee Program Borrower Agreement, dated as of March 6, 2018, by and between BL Acquisition II Inc. in favor of the Export Import Bank of the United States and Western Alliance Bank	X			
21.1	Subsidiaries of the Registrant	X			
23.1	Consent of Independent Registered Public Accounting Firm, BDO USA, LLP	X			
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14 and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended	X			
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14 and Rule 15d-14(a) of the Securities Exchange Act of 1934, as amended	X			
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	**			
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	**			
101	The following financial information from the Company's Annual Report on Form 10-K, for the year ended December 31, 2017, formatted in eXtensible Business Reporting Language: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations and Comprehensive Loss, (iii) Consolidated Statements of Stockholders' Equity (Deficit), (iv) Consolidated Statements of Cash Flows, (v) Notes to Consolidated Financial Statements	X			

† Confidential treatment was granted for certain confidential portions of this exhibit pursuant to Rule 24b-2 under the Securities Exchange Act of 1934. In accordance with Rule 24b-2, these confidential portions were omitted from this exhibit and filed separately with the Securities and Exchange Commission.

* Management contract or compensatory plan or arrangement.

** Furnished herewith.

SIGNATURES

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

Dated: March 14, 2018

BIOLASE, INC.,
a Delaware Corporation
(registrant)

By: /s/ HAROLD C. FLYNN, JR.

Harold C. Flynn, Jr.
President and Chief Executive Officer

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

Signature	Title	Date
<u> /s/ HAROLD C. FLYNN, JR. </u> Harold C. Flynn, Jr.	President and Chief Executive Officer (Principal Executive Officer) and Director	March 14, 2018
<u> /s/ JOHN R. BEAVER </u> John R. Beaver	Senior Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 14, 2018
<u> /s/ DR. JONATHAN T. LORD </u> Dr. Jonathan T. Lord	Director	March 14, 2018
<u> /s/ DR. RICHARD B. LANMAN </u> Dr. Richard B. Lanman	Director	March 14, 2018
<u> /s/ JAMES R. TALEVICH </u> James R. Talevich	Director	March 14, 2018

BIOLASE, INC.

Index to Consolidated Financial Statements and Schedule

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Consolidated Statements of Operations and Comprehensive Loss for the years ended December 31, 2017, 2016, and 2015	F-4
Consolidated Statements of Stockholders' Equity for the years ended December 31, 2017, 2016, and 2015	F-5
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Notes to Consolidated Financial Statements	F-8
SCHEDULE	
Schedule numbered in accordance with Rule 5.04 of Regulation S-X:	
II. Consolidated Valuation and Qualifying Accounts and Reserves for the years ended December 31, 2017, 2016 and 2015	S-1

All Schedules, except Schedule II, have been omitted as the required information is shown in the consolidated financial statements, or notes thereto, or the amounts involved are not significant or the schedules are not applicable.

Report of Independent Registered Public Accounting Firm

Shareholders and Board of Directors
BIOLASE, Inc.
Irvine, California

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of BIOLASE, Inc. and subsidiaries (collectively, the “Company”) as of December 31, 2017 and 2016, the related consolidated statements of operation and comprehensive loss, stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes and schedule listed in the index appearing under Item 15(a)(2) (collectively referred to as the “consolidated financial statements”). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company and subsidiaries at December 31, 2017 and 2016, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

Going Concern Uncertainty

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has suffered recurring losses from operations and has negative cash flows from operations for each of the three years in the period ended December 31, 2017. These factors, among others, raise substantial doubt about its ability to continue as a going concern. Management’s plans in regard to these matters are also described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ BDO USA, LLP

We have served as the Company's auditor since 2005.

Costa Mesa, California

March 14, 2018

BIOLASE, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

	December 31,	
	2017	2016
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 11,645	\$ 8,924
Restricted cash	251	251
Accounts receivable, less allowance of \$802 and \$1,209 in 2017 and 2016, respectively	10,124	9,784
Inventory, net	12,298	13,523
Prepaid expenses and other current assets	1,732	1,505
Total current assets	36,050	33,987
Property, plant, and equipment, net	3,674	4,478
Goodwill	2,926	2,926
Other assets	334	550
Total assets	\$ 42,984	\$ 41,941
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 5,109	\$ 9,125
Accrued liabilities	5,609	5,778
Customer deposits	27	101
Deferred revenue, current portion	2,625	3,010
Total current liabilities	13,370	18,014
Deferred income taxes, net	104	798
Deferred revenue, long-term	11	23
Warranty accrual, long-term	70	773
Other liabilities, long-term	169	268
Total liabilities	13,724	19,876
Commitments, contingencies and subsequent events (Notes 6 and 10)		
Stockholders' equity:		
Preferred stock, par value \$0.001 per share; 1,000 shares authorized, 0 shares issued and outstanding as of December 31, 2017 and 2016, respectively	—	—
Common stock, par value \$0.001 per share; 200,000 and 100,000 shares authorized, 102,340 and 67,566 shares issued and outstanding as of December 31, 2017 and 2016, respectively	102	68
Additional paid-in capital	224,910	201,198
Accumulated other comprehensive loss	(576)	(876)
Accumulated deficit	(195,176)	(178,325)
Total stockholders' equity	29,260	22,065
Total liabilities and stockholders' equity	\$ 42,984	\$ 41,941

See accompanying notes to consolidated financial statements.

BIOLASE, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

(in thousands, except per share data)

	Years Ended December 31,		
	2017	2016	2015
Products and services revenue	\$ 46,798	\$ 51,661	\$ 48,269
License fees and royalty revenue	128	149	206
Net revenue	46,926	51,810	48,475
Cost of revenue	31,800	31,502	32,525
Gross profit	15,126	20,308	15,950
Operating expenses:			
Sales and marketing	16,718	17,018	18,696
General and administrative	9,712	10,453	10,256
Engineering and development	6,229	7,799	7,283
Disposal of internally developed software	505	—	—
Excise tax	—	—	361
Legal settlement	—	—	(731)
Total operating expenses	33,164	35,270	35,865
Loss from operations	(18,038)	(14,962)	(19,915)
Gain (loss) on foreign currency transactions	563	(332)	(259)
Interest income, net	42	74	74
Non-operating gain (loss), net	605	(258)	(185)
Loss before income tax provision	(17,433)	(15,220)	(20,100)
Income tax (benefit) provision	(582)	151	178
Net loss	(16,851)	(15,371)	(20,278)
Other comprehensive income (loss) items:			
Foreign currency translation adjustments	300	(75)	(244)
Comprehensive loss	\$ (16,551)	\$ (15,446)	\$ (20,522)
Net loss	\$ (16,851)	\$ (15,371)	\$ (20,278)
Deemed dividend on convertible preferred stock	(3,978)	(2,184)	—
Net loss attributable to common stockholders	\$ (20,829)	\$ (17,555)	\$ (20,278)
Net loss per share attributable to common stockholders:			
Basic	\$ (0.28)	\$ (0.29)	\$ (0.35)
Diluted	\$ (0.28)	\$ (0.29)	\$ (0.35)
Shares used in the calculation of net loss per share:			
Basic	73,759	60,664	58,189
Diluted	73,759	60,664	58,189

See accompanying notes to consolidated financial statements.

BIOLASE, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands)

	Common Stock and Additional Paid-in Capital		Convertible Preferred Stock		Accumulated Other Comprehensive Loss	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount	Shares	Amount			
Balances, January 1, 2015	58,115	\$ 185,289	—	\$ —	\$ (557)	\$ (142,676)	\$ 42,056
Exercise of stock options, net	113	44	—	—	—	—	44
Stock-based compensation	—	3,350	—	—	—	—	3,350
Cost of issuance	—	(3)	—	—	—	—	(3)
Net loss	—	—	—	—	—	(20,278)	(20,278)
Foreign currency translation adjustment	—	—	—	—	(244)	—	(244)
Balances, December 31, 2015	58,228	188,680	—	—	(801)	(162,954)	24,925
Exercise of stock options, net	—	1	—	—	—	—	1
Stock-based compensation	—	3,065	—	—	—	—	3,065
Issuance of stock from RSUs, net	489	—	—	—	—	—	—
Issuance of Series C participating convertible preferred stock and warrants, net of issuance cost of \$480	—	1,092	88	8,428	—	—	9,520
Beneficial conversion feature of Series C participating convertible preferred stock	—	1,092	—	(1,092)	—	—	—
Deemed dividend related to beneficial conversion feature of Series C participating convertible preferred stock	—	(2,184)	—	2,184	—	—	—
Issuance of common stock upon conversion of Series C participating convertible preferred stock	8,849	9,520	(88)	(9,520)	—	—	—
Net loss	—	—	—	—	—	(15,371)	(15,371)
Foreign currency translation adjustment	—	—	—	—	(75)	—	(75)
Balances, December 31, 2016	67,566	201,266	—	—	(876)	(178,325)	22,065
Exercise of stock options, net	—	3	—	—	—	—	3
Stock-based compensation	—	2,145	—	—	—	—	2,145
Issuance of stock from RSUs, net	406	—	—	—	—	—	—
Issuance of Series D participating convertible preferred stock and warrants, net of issuance cost of \$251	—	2,026	81	8,214	—	—	10,240
Beneficial conversion feature of Series D participating convertible preferred stock	—	1,952	—	(1,952)	—	—	—
Deemed dividend related to beneficial conversion feature of Series D participating convertible preferred stock	—	(3,978)	—	3,978	—	—	—

Issuance of common stock upon conversion of Series D participating convertible preferred stock	8,065	10,240	(81)	(10,240)	—	—	—
Issuance of stock from rights offering, net	26,303	11,358	—	—	—	—	11,358
Net loss	—	—	—	—	—	(16,851)	(16,851)
Foreign currency translation adjustment	—	—	—	—	300	—	300
Balances, December 31, 2017	<u>102,340</u>	<u>\$ 225,012</u>	<u>—</u>	<u>\$ —</u>	<u>\$ (576)</u>	<u>\$ (195,176)</u>	<u>\$ 29,260</u>

See accompanying notes to consolidated financial statements.

BIOLASE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Years Ended December 31,		
	2017	2016	2015
Cash Flows From Operating Activities:			
Net loss	\$ (16,851)	\$ (15,371)	\$ (20,278)
Adjustments to reconcile net loss to net cash and cash equivalents used in operating activities:			
Depreciation and amortization	1,203	1,048	880
Loss (gain) on disposal of assets, net	505	(2)	6
Provision (recovery) for bad debts, net	40	(118)	86
Provision for inventory excess and obsolescence	623	272	647
Provision for sales returns allowance	—	—	100
Stock-based compensation	2,207	3,065	3,350
Deferred income taxes	(694)	60	61
Earned interest income, net	(42)	(70)	(74)
Changes in operating assets and liabilities:			
Restricted cash	—	(51)	(200)
Accounts receivable	(337)	(644)	(52)
Inventory	419	(1,989)	(705)
Prepaid expenses and other current assets	(11)	79	(65)
Customer deposits	(74)	16	(27)
Accounts payable and accrued liabilities	(5,003)	3,322	(640)
Accrued legal settlement	—	—	(1,664)
Deferred revenue	(397)	(264)	803
Net cash and cash equivalents used in operating activities	<u>(18,412)</u>	<u>(10,647)</u>	<u>(17,772)</u>
Cash Flows From Investing Activities:			
Purchases of property, plant, and equipment	(747)	(1,414)	(1,803)
Proceeds from disposal of property, plant, and equipment	—	—	25
Net cash and cash equivalents used in investing activities	<u>(747)</u>	<u>(1,414)</u>	<u>(1,778)</u>
Cash Flows From Financing Activities:			
Principal payments under capital lease obligation	(146)	(171)	(107)
Proceeds from equity offerings, net of expenses	21,761	9,520	—
Deposit on capital lease	—	—	(42)
Proceeds from exercise of stock options	3	1	44
Net cash and cash equivalents provided by (used in) financing activities	<u>21,618</u>	<u>9,350</u>	<u>(105)</u>
Effect of exchange rate changes	262	(64)	(206)
Increase (decrease) in cash and cash equivalents	2,721	(2,775)	(19,861)
Cash and cash equivalents, beginning of year	8,924	11,699	31,560
Cash and cash equivalents, end of year	<u>\$ 11,645</u>	<u>\$ 8,924</u>	<u>\$ 11,699</u>
Supplemental cash flow disclosure - Cash Paid:			
Interest paid	\$ 1	\$ 4	\$ 4
Income taxes paid	\$ 164	\$ 76	\$ 57
Supplemental cash flow disclosure - Non-cash:			
Assets acquired under capital lease	\$ —	\$ —	\$ 378
Accrued capital expenditures and tenant improvement allowance	\$ 102	\$ 251	\$ 1,137

See accompanying notes to consolidated financial statements.

BIOLASE, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENT

NOTE 1 — BASIS OF PRESENTATION

The Company

BIOLASE, Inc. (“BIOLASE” and, together with its consolidated subsidiaries, the “Company”) incorporated in Delaware in 1987, is a medical device company that develops, manufactures, markets, and sells laser systems in dentistry and medicine and also markets, sells, and distributes dental imaging equipment, including three-dimensional CAD/CAM intra-oral scanners and digital dentistry software.

Use of Estimates

The preparation of these consolidated financial statements in conformity with generally accepted accounting principles in the United States of America (“GAAP”) requires the Company to make estimates and assumptions that affect amounts reported in the consolidated financial statements and the accompanying notes. Significant estimates in these consolidated financial statements include allowances on accounts receivable, inventory, and deferred taxes, as well as estimates for accrued warranty expenses, goodwill and the ability of goodwill to be realized, revenue deferrals, effects of stock-based compensation and warrants, contingent liabilities, and the provision or benefit for income taxes. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may differ materially from those estimates.

Fair Value of Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the principal market (or, if none exists, the most advantageous market) for the specific asset or liability at the measurement date (referred to as the “exit price”). The fair value is based on assumptions that market participants would use, including a consideration of non-performance risk. Under the accounting guidance for fair value hierarchy, there are three levels of measurement inputs. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are observable, either directly or indirectly. Level 3 inputs are unobservable due to little or no corroborating market data.

The Company’s financial instruments, consisting of cash and cash equivalents, accounts receivable, accounts payable, capital lease obligations, and accrued liabilities, approximate fair value because of the liquid or short-term nature of these items.

Rights Offering

The Company completed a rights offering on December 5, 2017 by selling 26,302,703 shares of common stock. Gross proceeds were approximately \$12.0 million, and net proceeds, after offering expenses of approximately \$0.6 million, were approximately \$11.4 million. Certain affiliates of Larry Feinberg and an affiliate of Jack Schuler exercised their basic subscription rights and over-subscription privilege in the rights offering and purchased a total of 10,745,614 shares and 10,964,912 shares of common stock, respectively, on the same terms as all other participants. The Company plans to use the net proceeds from the rights offering for general working capital needs.

Convertible Preferred Stock and Warrant Transactions

2017 Private Placement

On April 18, 2017, the Company completed a private placement with several institutional and individual investors, and certain of its directors and officers, under which the Company sold an aggregate of 80,644 shares of BIOLASE Series D Participating Convertible Preferred Stock, par value \$0.001 per share (“Preferred Stock”), and warrants (the “2017 Warrants”) to purchase up to an aggregate of 3,925,871 unregistered shares of BIOLASE common stock at an exercise price of \$1.80 per share, subject to customary anti-dilution adjustments. Each share of Preferred Stock converted automatically into 100 shares of BIOLASE common stock upon receipt of stockholder approval on June 30, 2017, reflecting a conversion price equal to \$1.24 per share, which was the closing price of BIOLASE common stock quoted on the NASDAQ Capital Market on April 10, 2017. On June 30, 2017, BIOLASE’s stockholders also approved the issuance of BIOLASE common stock related to the exercise of the 2017 Warrants by certain holders whose 2017 Warrants were subject to a beneficial ownership limitation.

The 2017 Warrants became exercisable on October 18, 2017 and expire on April 18, 2022, or, if earlier, five business days after the Company delivers notice that the closing price per share of BIOLASE common stock exceeded the exercise price of \$1.80 per share for 30 consecutive trading days during the exercise period. Gross proceeds from the sale were approximately \$10.5

million, and net proceeds, after offering expenses of approximately \$0.3 million, were approximately \$10.2 million. The Company used the proceeds from the private placement for working capital and general corporate purposes. In connection with the registration rights granted to these investors, the Company filed with the SEC a registration statement on Form S-3, which was declared effective on August 24, 2017.

In accordance with applicable accounting standards, the \$10.5 million gross proceeds from the private placement described above were allocated to the Preferred Stock and the 2017 Warrants in the amount of \$8.2 million and \$2.3 million, respectively. The allocation was based on the relative fair values of the underlying BIOLASE common stock and the 2017 Warrants as of the commitment date, with the fair value of the 2017 Warrants determined using a Black Scholes model. Assumptions used in the Black-Scholes model include an expected term of five years, a risk-free rate of 1.90% and a dividend yield of 0%. This transaction resulted in a discount from allocation of proceeds to separable instruments of \$2.0 million and a beneficial conversion to BIOLASE common stock with a value of \$2.0 million, which have been reflected as a deemed distribution to preferred shareholders for the year ended December 31, 2017.

2016 Private Placement

On August 8, 2016, the Company completed a private placement with several institutional and individual investors, and certain of its directors and officers, under which the Company sold an aggregate of 88,494 shares of BIOLASE Series C Participating Convertible Preferred Stock ("Series C Preferred Stock") and warrants ("2016 Warrants") to purchase up to an aggregate of 2,035,398 unregistered shares of BIOLASE common stock at an exercise price of \$2.00 per share. Each share of Series C Preferred Stock converted automatically into 100 shares of BIOLASE common stock, upon receipt of stockholder approval on September 30, 2016, reflecting a conversion price equal to \$1.13 per share, which was the closing price of BIOLASE common stock quoted on the NASDAQ Capital Market on July 29, 2016. On September 30, 2016, BIOLASE's stockholders also approved the issuance of BIOLASE common stock related to the exercise of the 2016 Warrants by certain holders whose 2016 Warrants were subject to a beneficial ownership limitation. Gross proceeds from the sale were \$10.0 million, and net proceeds, after offering expenses of approximately \$0.5 million, were approximately \$9.5 million.

The 2016 Warrants became exercisable on February 8, 2017 and expire on August 8, 2021. The Company used the proceeds from the sale for working capital and general corporate purposes. In connection with the registration rights granted to these investors, the Company filed a registration statement on Form S-3 with the SEC, which was declared effective on November 3, 2016.

In accordance with applicable accounting standards, the \$10.0 million gross proceeds from sale were allocated to the Series C Preferred Stock and the 2016 Warrants in the amount of \$8.9 million and \$1.1 million, respectively. The allocation was based on the relative fair values of the underlying BIOLASE common stock and the 2016 Warrants as of the commitment date, with the fair value of the 2016 Warrants determined using a Black Scholes model. Assumptions used in the Black-Scholes model include an expected term of five years, risk-free rate of 1.03% and a dividend yield of 0%. This transaction resulted in a discount from allocation of proceeds to separable instruments of \$1.1 million and a beneficial conversion to BIOLASE common stock with a value of \$1.1 million, which have been reflected as a deemed distribution to preferred shareholders in the year ended December 31, 2016.

Concentration of Credit Risk, Interest Rate Risk and Foreign Currency Exchange Rate

Financial instruments which potentially expose the Company to a concentration of credit risk consist principally of cash and cash equivalents, restricted cash, and trade accounts receivable. The Company maintains its cash and cash equivalents and restricted cash with established commercial banks. At times, balances may exceed federally insured limits. To minimize the risk associated with trade accounts receivable, management performs ongoing credit evaluations of customers' financial condition and maintains relationships with the Company's customers that allow management to monitor current changes in business operations so the Company can respond as needed. The Company does not, generally, require customers to provide collateral before it sells them its products. However, the Company has required certain distributors to make prepayments for significant purchases of products.

Substantially all of the Company's revenue is denominated in U.S. dollars, including sales to international distributors. Only a small portion of its revenue and expenses is denominated in foreign currencies, principally the Euro and Indian Rupee. The Company's foreign currency expenditures primarily consist of the cost of maintaining offices, consulting services, and employee-related costs. During the years ended December 31, 2017, 2016, and 2015, the Company did not enter into any hedging contracts. Future fluctuations in the value of the U.S. dollar may affect the price competitiveness of the Company's products outside the U.S.

Liquidity and Management's Plans

The Company has reported recurring losses from operations and has not generated cash from operations for the three years ended December 31, 2017. During the years ended December 31, 2017, 2016 and 2015, the principal sources of liquidity for the Company were its net proceeds from the December 5, 2017, April 18, 2017 and August 8, 2016 sales by the Company of \$11.4 million, \$10.2 million, and \$9.5 million, respectively, of unregistered shares of BIOLASE equity securities. The Company's recurring losses, level of cash used in operations, potential need for additional capital, and the uncertainties surrounding our ability to raise additional capital, raises substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

At December 31, 2017, the Company had approximately \$22.7 million in working capital. The Company's principal sources of liquidity at December 31, 2017 consisted of approximately \$11.9 million in cash, cash equivalents, and restricted cash, and \$10.1 million of net accounts receivable.

In order for the Company to continue operations beyond the next 12 months and be able to discharge its liabilities and commitments in the normal course of business, the Company must increase sales of its products, control or potentially reduce expenses and establish profitable operations in order to generate cash from operations or obtain additional funds when needed.

Additional capital requirements may depend on many factors, including, among other things, the rate at which the Company's business grows, demands for working capital, manufacturing capacity, and any acquisitions that the Company may pursue. From time to time, the Company could be required, or may otherwise attempt, to raise capital through either equity or debt offerings. The Company cannot provide assurance that it will be able to successfully enter into any such equity or debt financings in the future or that the required capital would be available on acceptable terms, if at all, or that any such financing activity would not be dilutive to its stockholders.

NOTE 2 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturities of three months or less when purchased, as cash equivalents. Cash equivalents are carried at cost, which approximates fair market value.

Restricted Cash

Restricted cash represents a revolving 90-day certificate of deposit maintained by the Company as collateral in connection with corporate credit cards. At December 31, 2017 and 2016, the restricted cash balance was \$251,000 and \$251,000, respectively.

Accounts Receivable

Trade accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in its existing accounts receivable. The Company evaluates its allowance for doubtful accounts based upon its knowledge of customers and their compliance with credit terms. The evaluation process includes a review of customers' accounts on a regular basis, which incorporates input from sales, service, and finance personnel. The review process also evaluates all account balances with amounts past due and other specific amounts for which information obtained indicates that the balance may be uncollectible. The allowance for doubtful accounts is adjusted based on such evaluation, with a corresponding provision included in general and administrative expenses. Account balances are charged off against the allowance when it is probable the receivable will not be recovered. The Company does not have any off-balance-sheet credit exposure related to its customers.

Inventory

The Company values inventory at the lower of cost or net realizable value, with cost determined using the first-in, first-out method. The carrying value of inventory is evaluated periodically for excess quantities and obsolescence. Management evaluates quantities on hand, physical condition, and technical functionality as these characteristics may be impacted by anticipated customer demand for current products and new product introductions. The allowance is adjusted based on such evaluation, with a corresponding provision included in cost of revenue. Abnormal amounts of idle facility expenses, freight, handling costs and wasted material are recognized as current period charges, and the Company's allocation of fixed production overhead is based on the normal capacity of its production facilities.

Property, Plant, and Equipment

Property, plant, and equipment is stated at acquisition cost less accumulated depreciation. Maintenance and repairs are expensed as incurred. Upon sale or disposition of assets, any gain or loss is included in the consolidated statements of operations.

The cost of property, plant, and equipment is depreciated using the straight-line method over the following estimated useful lives of the respective assets, except for leasehold improvements, which are depreciated over the lesser of the estimated useful lives of the respective assets or the related lease terms.

Building	30 years
Leasehold improvements	3 to 5 years
Equipment and computers	3 to 5 years
Furniture and fixtures	5 years

Depreciation expense for the years ended December 31, 2017, 2016, and 2015 totaled approximately \$1,203,000, \$997,000, and \$817,000, respectively.

Goodwill and Other Intangible Assets

Goodwill is not subject to amortization but is evaluated for impairment annually or whenever events or changes in circumstances indicate that the asset might be impaired. The Company operates in one reporting and operating unit; therefore goodwill is tested for impairment at the consolidated level against the fair value of the Company. The fair value of a reporting unit refers to the amount at which the unit as a whole could be bought or sold in a current transaction between willing parties. Quoted market prices in active markets are the best evidence of fair value and are used as the basis for measurement, if available. Management assesses potential impairment on an annual basis on June 30th and compares the Company's market capitalization to its carrying amount, including goodwill. A significant decrease in the Company's stock price could indicate a material impairment of goodwill which, after further analysis, could result in a material charge to operations. If goodwill is considered impaired, the impairment loss to be recognized is measured by the amount by which the carrying amount of the goodwill exceeds the implied fair value of that goodwill. Inherent in the Company's fair value determinations are certain judgments and estimates, including projections of future cash flows, the discount rate reflecting the inherent risk in future cash flows, the interpretation of current economic indicators and market valuations, and strategic plans with regard to operations. A change in these underlying assumptions could cause a change in the results of the tests, which could cause the fair value of the reporting unit to be less than its respective carrying amount.

Costs incurred to acquire and successfully defend patents, and costs incurred to acquire trademarks and trade names are capitalized. Costs related to the internal development of technologies that are ultimately patented are expensed as incurred. Intangible assets, except those determined to have an indefinite life, are amortized using the straight-line method or over management's best estimate of the pattern of economic benefit over the estimated useful life of the assets. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable.

Long-Lived Assets

The carrying values of long-lived assets, including intangible assets subject to amortization, are reviewed when indicators of impairment, such as reductions in demand or significant economic slowdowns, are present. Reviews are performed to determine whether carrying value of an asset is impaired based on comparisons to undiscounted expected future cash flows. If this comparison indicates that there is impairment, the impaired asset is written down to fair value, which is typically calculated using discounted expected future cash flows. Impairment is based on the excess of the carrying amount over the fair value of those assets.

Other Comprehensive (Loss) Income

Other comprehensive (loss) income encompasses the change in equity from transactions and other events and circumstances from non-owner sources and is included as a component of stockholders' equity but is excluded from net (loss) income. Accumulated other comprehensive (loss) income is comprised of foreign currency translation adjustments.

Foreign Currency Translation and Transactions

Transactions of the Company's German, Spanish, Australian, and Indian subsidiaries are denominated in their local currencies. The results of operations and cash flows are translated at average exchange rates during the period, and assets and liabilities are translated at end-of-period exchange rates. Translation gains or losses are shown as a component of accumulated other comprehensive (loss) income in stockholders' equity. Income and losses resulting from foreign currency transactions, which are denominated in a currency other than the entity's functional currency, are included in comprehensive loss in the consolidated statements of operations.

Revenue Recognition

The Company's products are sold in North America directly to customers through its field sales force and through non-exclusive distributors. The Company sells its products internationally through exclusive and non-exclusive distributors as well as directly to customers in certain countries. Sales are recorded upon shipment from the Company's facility, and payment of its invoices is generally due within 90 days or less. Internationally, the Company primarily sells products through independent distributors. Revenue is recorded based on four basic criteria that must be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred and title and the risks and rewards of ownership have been transferred to the customer or services have been rendered; (3) the price is fixed or determinable; and (4) collectability is reasonably assured. Revenue is recorded for all sales upon shipment assuming all other revenue recognition criteria are met.

Sales of the Company's laser systems include separate deliverables consisting of the product, disposables used with the laser systems, installation, and training. For sale of deliverables that are part of a multiple-element arrangement, the Company applies a method that approximates the relative selling price method, which requires that arrangement consideration be allocated at the inception of an arrangement to all deliverables using the relative selling price method. This requires the Company to use estimated selling prices of each of the deliverables in the total arrangement. The sum of those prices is then compared to the arrangement, and any difference is applied to the separate deliverable ratably. This method also establishes a selling price hierarchy for determining the selling price of a deliverable, which includes: (i) vendor-specific objective evidence ("VSOE"), if available, (ii) third-party evidence if VSOE is not available, and (iii) estimated selling price if neither VSOE nor third-party evidence is available. VSOE is determined based on the value the Company sells the undelivered element to a customer as a stand-alone product. Revenue attributable to the undelivered elements is included in deferred revenue when the product is shipped and is recognized when the related service is performed. Disposables not shipped at time of sale and installation services are typically shipped or installed within 30 days. Training is included in deferred revenue when the product is shipped and is recognized when the related service is performed or upon the appropriate expiration of time offered under the agreement. Deferred revenue attributable to undelivered elements, which primarily consists of training, totaled approximately \$1.0 million and \$1.4 million as of December 31, 2017 and 2016, respectively.

Key judgments of the Company's revenue recognition include the collectability of payment from the customer, the satisfaction of all elements of the arrangement having been delivered, and that no additional customer credits and discounts are needed. The Company evaluates the customer's credit worthiness prior to the shipment of the product. Based on the assessment of the credit information available, the Company may determine the credit risk is higher than normally acceptable, and will either decline the purchase or defer the revenue until payment is reasonably assured. Future obligations required at the time of sale may also cause the Company to defer the revenue until the obligation is satisfied.

Although all sales are final, the Company accepts returns of products in certain, limited circumstances and records a provision for sales returns based on historical experience concurrent with the recognition of revenue. The sales returns allowance is recorded as a reduction of accounts receivable and revenue. As of December 31, 2017 and 2016, \$210,000 and \$210,000, respectively, was recorded as a reduction of accounts receivable for sales returns.

Extended warranty contracts, which are sold to laser and certain imaging customers, are recorded as revenue on a straight-line basis over the period of the contracts, which is typically one year. Included in deferred revenue for each of the years ended December 31, 2017 and 2016, was approximately \$1.6 million and \$1.5 million, respectively, for extended warranty contracts.

For sales transactions involving used laser trade-ins, the Company records the purchased trade-ins as inventory at the fair value of the asset surrendered with the offset to accounts receivable. In determining the estimated fair value of used laser trade-ins, the Company makes an assessment of usable parts and key components and considers the ultimate resale value of the certified pre-owned (or “CPO”) laser with applicable margins. The Company sells these CPO laser trade-ins as refurbished lasers. Trade-in rights are not established or negotiated with customers during the initial sales transaction of the original lasers. Trade-in rights are promotional events used at management’s discretion to encourage existing laser customers to purchase new lasers. A customer is not required to trade in a laser nor is the Company required to accept a trade-in. However, the promotional value offered in exchange for the trade-in laser is not offered without a laser trade-in. The transaction is treated as a monetary transaction as each sale transaction involving a customer trade-in includes significant boot of greater than 25% of the fair value of the exchange. As a monetary transaction, the sale is recognized following the Company’s laser system revenue recognition policy. There have been no sales transactions in which the cash consideration was less than 25% of the total transaction value.

The Company recognizes revenue for royalties under licensing agreements for its patented technology when the product using its technology is sold. The Company estimates and recognizes the amount earned based on historical performance and current knowledge about the business operations of its licensees. The Company’s estimates have been consistent with amounts historically reported by the licensees. Licensing revenue related to exclusive licensing arrangements is recognized concurrent with the related exclusivity period.

From time to time, the Company may offer sales incentives and promotions on its products. The cost of sales incentives are recorded at the date at which the related revenue is recognized as a reduction in revenue, an increase in cost of goods sold or a selling expense, as applicable, or later, in the case of incentives offered after the initial sale has occurred.

Provision for Warranty Expense

The Company provides warranties against defects in materials and workmanship of its laser systems for specified periods of time. For the years ended December 31, 2017 and 2016, laser systems sold domestically were covered by the warranty for a period of up to two years from the date of sale by the Company or the distributor to the end-user. In 2017, for Waterlase systems sold domestically and purchased in 2017 or later, the Company decreased the warranty period from two years to one year. Laser systems sold internationally were covered by the warranty for a period of up to 28 months from the date of sale to the international distributor. In 2017, for Waterlase systems sold internationally and purchased in 2017 or later, the Company decreased the warranty period from 28 months to 16 months. Estimated warranty expenses are recorded as an accrued liability with a corresponding provision to cost of revenue. This estimate is recognized concurrent with the recognition of revenue on the sale to the distributor or end-user. Warranty expenses expected to be incurred after one year from the time of sale to the distributor are classified as a long-term warranty accrual. The Company’s overall accrual is based on its historical experience and management’s expectation of future conditions, taking into consideration the location and type of customer and the type of laser, which directly correlate to the materials and components under warranty, the duration of the warranty period, and the logistical costs to service the warranty. Additional factors that may impact the Company’s warranty accrual include changes in the quality of materials, leadership and training of the production and services departments, knowledge of the lasers and workmanship, training of customers, and adherence to the warranty policies. Additionally, an increase in warranty claims or in the costs associated with servicing those claims would likely result in an increase in the accrual and a decrease in gross profit. All imaging products are initially covered by the manufacturer’s warranties. However, the Company offers extended warranties on certain imaging products.

Changes in the initial product warranty accrual and the expenses incurred under the Company’s initial and extended warranties for the years ended December 31 are included within accrued liabilities on the Consolidated Balance Sheets and were as follows (in thousands):

	Years Ended December 31,		
	2017	2016	2015
Initial warranty accrual, beginning balance	\$ 1,706	\$ 2,188	\$ 1,449
Provision for estimated warranty cost	492	348	1,715
Warranty expenditures	(1,008)	(830)	(976)
Initial warranty accrual, ending balance	1,190	1,706	2,188
Less warranty accrual, long-term	70	773	843
Total warranty accrual, current portion	<u>\$ 1,120</u>	<u>\$ 933</u>	<u>\$ 1,345</u>

Shipping and Handling Costs and Revenues

Shipping and handling costs are expensed as incurred and are recorded as a component of cost of revenue. Charges to customers for shipping and handling are included as a component of revenue.

Advertising Costs

Advertising costs are expensed as incurred and totaled approximately \$298,000, \$351,000, and \$929,000 for the years ended December 31, 2017, 2016, and 2015, respectively.

Engineering and Development

Engineering and development expenses are generally expensed as incurred and consist of engineering personnel salaries and benefits, prototype supplies, contract services, and consulting fees related to product development.

Stock-Based Compensation

During the years ended December 31, 2017, 2016, and 2015, the Company recognized compensation cost related to stock options of \$2.2 million, \$3.1 million, and \$3.4 million, respectively, based on the grant-date fair value. The following table summarizes the income statement classification of compensation expense associated with share-based payments (in thousands):

	Years Ended December 31,		
	2017	2016	2015
Cost of revenue	\$ 207	\$ 226	\$ 333
Sales and marketing	235	477	679
General and administrative	1,469	2,051	2,020
Engineering and development	296	311	318
	<u>\$ 2,207</u>	<u>\$ 3,065</u>	<u>\$ 3,350</u>

As of December 31, 2017 and 2016, the Company had \$3.4 million and \$4.0 million, respectively, of total unrecognized compensation cost, net of estimated forfeitures, related to unvested share-based compensation arrangements granted under its existing plans. The \$3.4 million in cost is expected to be recognized over a weighted-average period of 2.0 years as of December 31, 2017.

The Company uses the Black-Scholes option valuation model for estimating the fair value of options. This option-pricing model requires the Company to make several assumptions regarding the key variables used to calculate the fair value of its stock options. The risk-free interest rate used is based on the U.S. Treasury yield curve in effect for the expected lives of the options at their dates of grant. Since July 1, 2005, the Company has used a dividend yield of zero, as it does not intend to pay cash dividends on its common stock in the foreseeable future. The most critical assumptions used in calculating the fair value of stock options is the expected life of the option and the expected volatility of BIOLASE common stock. The expected life is calculated in accordance with the simplified method, whereby for service-based awards the expected life is calculated as a midpoint between the vesting date and expiration date. The Company uses the simplified method, as there is not a sufficient history of share option exercises. For performance-based awards, the expected life equals the life of the award. Management believes that the historic volatility of BIOLASE common stock is a reliable indicator of future volatility, and accordingly, a stock volatility factor based on the historical volatility of BIOLASE common stock over a lookback period of the expected life is used in approximating the estimated volatility of new stock options. Compensation expense is recognized using the straight-line method for all service-based employee awards and graded amortization for all performance-based awards. Compensation expense is recognized only for those options expected to vest, with forfeitures estimated at the date of grant based on historical experience and future expectations. Forfeitures are estimated at the time of the grant and revised in subsequent periods as actual forfeitures differ from those estimates. BIOLASE applied a forfeiture rate of 6.38% and 40.90% to awards granted to executives and employees, respectively, during the year ended December 31, 2017.

The stock option fair values, under the 2002 Plan, were estimated using the Black-Scholes option-pricing model with the following assumptions:

	2017	2016	2015
Expected term (years)	5.51	5.96	5.80
Volatility	79%	86%	90%
Annual dividend per share	\$ —	\$ —	\$ —
Risk-free interest rate	1.99%	1.39%	1.64%

Excise Tax

Commencing January 1, 2013, certain of the Company's product sales have been subject to the medical device excise tax. The Company has included such taxes separately as a component of operating expense. Effective beginning 2016, the excise tax imposed on the sale of medical devices has been suspended for the calendar years 2016 and 2017. Effective beginning 2018, the excise tax imposed on the sale of medical devices has been suspended through January 1, 2020.

Income Taxes

Differences between accounting for income taxes for financial statement purposes and accounting for tax return purposes are stated as deferred tax assets or deferred tax liabilities in the accompanying consolidated financial statements. The provision for income taxes represents the tax payable for the period and the change during the period in deferred tax assets and liabilities. The Company establishes a valuation allowance when it is more likely than not that the deferred tax assets will not be realized.

The income tax provisions for the years ended December 31, 2017, 2016, and 2015 were calculated using the discrete year-to-date method. See *Note 5 – Income Taxes* for additional disclosures related to the Company's income tax.

Net Loss Per Share — Basic and Diluted

Basic net income (loss) per share is computed by dividing income (loss) available to common stockholders by the weighted-average number of common shares outstanding for the period. In computing diluted net income (loss) per share, the weighted average number of shares outstanding is adjusted to reflect the effect of potentially dilutive securities.

Outstanding stock options, restricted stock units and warrants to purchase approximately 16,918,000, 20,537,000, and 17,371,000 shares were not included in the calculation of diluted loss per share amounts for the years ended December 31, 2017, 2016, and 2015, respectively, as their effect would have been anti-dilutive.

Recent Accounting Pronouncements

Changes to GAAP are established by the Financial Accounting Standards Board ("FASB") in the form of accounting standards updates ("ASUs") to the FASB's Accounting Standards Codification ("ASC").

The Company considers the applicability and impact of all ASUs. ASUs not listed below were assessed and determined not to be applicable or are expected to have minimal impact on the Company's consolidated financial position and results of operations.

Adopted Accounting Standards

In July 2015, the FASB issued ASU No. 2015-11, Simplifying the Measurement of Inventory ("ASU 2015-11"), as part of its simplification initiative. The standard requires inventory within the scope of ASU 2015-11 to be measured using the lower of cost and net realizable value. The changes apply to all types of inventory, except those measured using the last-in, first-out method or the retail inventory method. The Company adopted ASU 2015-11 as of January 1, 2017. The adoption of ASU 2015-11 did not have a material effect on the Company's consolidated financial statements.

In November 2015, FASB issued ASU 2015-17, Income Taxes (Topic 740) ("ASC 2015-17"). Previously, deferred income tax liabilities and assets were required to be presented into current and noncurrent amounts in a classified statement of financial position. To simplify the presentation of deferred income taxes, the amendments in this ASU require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this ASU apply to all entities that present a classified statement of financial position. The Company adopted ASU 2015-17 as of January 1, 2017. The adoption of ASU 2015-17 did not have a material effect on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Compensation – Stock Compensation (Topic 718) (“ASU 2016-09”). The updated standard simplifies several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The standard requires the recognition of the income tax effects of awards in the income statement when the awards vest or are settled, thus eliminating additional paid in capital pools. The Company adopted ASU 2016-09 as of January 1, 2017, and made the accounting policy election to estimate the number of awards expected to vest for stock-based compensation expense. The adoption of ASU 2016-09 and related accounting policy election did not have a material effect on the Company’s consolidated financial statements.

Accounting Standards Not Yet Adopted

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (“ASU 2014-09”). The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. The standard is effective for annual periods beginning after December 15, 2017, and interim periods therein.

ASU 2014-09 supersedes existing guidance on revenue recognition with a five-step model for recognizing and measuring revenue from contracts with customers. The objective of the new standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries, and across capital markets. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The guidance also requires a number of disclosures regarding the nature, amount, timing, and uncertainty of revenue and the related cash flows. The guidance can be applied retrospectively to each prior reporting period presented (full retrospective method) or retrospectively with a cumulative effect adjustment to retained earnings for initial application of the guidance at the date of initial adoption (modified retrospective method). The Company adopted the new standard effective January 1, 2018. The timing and measurement of revenue recognition under the new standard will not be materially different than under the old standard.

In February 2016, FASB issued ASU 2016-02, Leases (“ASU 2016-02”). The new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the impact of its pending adoption of ASU 2016-02 on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230) (“ASU 2016-15”). The updated standard addresses eight specific cash flow issues with the objective of reducing diversity in practice. ASU 2016-15 is effective for public business entities for annual reporting periods beginning after December 15, 2017, including interim periods within those annual reporting periods. Early adoption is permitted. The Company is assessing the impact of the adoption of ASU 2016-15 on the Company’s consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Compensation – Stock Compensation (Topic 718) (“ASU 2017-09”). The updated standard clarifies when an entity must apply modification accounting to changes in the terms or conditions of a share-based payment award. ASU 2017-09 is effective for public business entities for annual reporting periods beginning after December 15, 2017, including interim periods within those annual reporting periods. Early adoption is permitted. The Company does not expect that the adoption of this standard will have a material effect on its consolidated financial statements.

NOTE 3 — SUPPLEMENTARY BALANCE SHEET INFORMATION

Accounts Receivable, net:

<u>(in thousands):</u>	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
Components of accounts receivable, net of allowances, are as follows:		
Trade	\$ 10,047	\$ 9,699
Royalties	71	62
Other	6	23
Total receivables, net	<u>\$ 10,124</u>	<u>\$ 9,784</u>

Accounts receivable is net of allowances for doubtful accounts of approximately \$0.8 million and \$1.2 million and sales returns of approximately \$210,000 and \$210,000 at December 31, 2017 and 2016, respectively.

Inventory, net:

<u>(in thousands):</u>	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
Components of inventory, net of allowances, are as follows:		
Raw materials	\$ 3,953	\$ 4,837
Work-in-process	1,162	2,261
Finished goods	7,183	6,425
Inventory, net	<u>\$ 12,298</u>	<u>\$ 13,523</u>

Inventory is net of a provision for excess and obsolete inventory totaling approximately \$1.9 million and \$1.7 million at December 31, 2017 and 2016, respectively.

Property, Plant, and Equipment, net:

<u>(in thousands):</u>	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
Components of property, plant, and equipment, net of depreciation, are as follows:		
Building	\$ 220	\$ 196
Leasehold improvements	2,005	2,003
Equipment and computers	6,883	6,163
Furniture and fixtures	634	599
Construction in progress	1,182	1,590
	10,924	10,551
Accumulated depreciation	(7,426)	(6,225)
	3,498	4,326
Land	176	152
Property, plant, and equipment, net	<u>\$ 3,674</u>	<u>\$ 4,478</u>

The cost basis of assets held under capital lease was \$378,000, which was fully depreciated as of December 31, 2017. The cost basis of assets held under capital lease was \$378,000 and the accumulated depreciation related to assets held under capital lease was \$227,000 as of December 31, 2016.

During 2017, the Company recognized a non-cash, pre-tax charge related to the disposal of internally developed software of \$505,000, primarily due to the decision to cancel future deployments of a new ERP system.

Accrued Liabilities:

(in thousands):	December 31,	
	2017	2016
Components of accrued liabilities are as follows:		
Payroll and benefits	\$ 2,115	\$ 2,147
Warranty accrual, current portion	1,120	933
Taxes	544	638
Accrued professional services	584	782
Accrued capital lease, current portion	—	159
Accrued insurance premium	870	906
Other	376	213
Accrued liabilities	<u>\$ 5,609</u>	<u>\$ 5,778</u>

Deferred Revenue:

(in thousands):	December 31,	
	2017	2016
Components of deferred revenue are as follows:		
Undelivered elements (training, installation, product and support services)	\$ 980	\$ 1,404
Extended warranty contracts	1,634	1,487
Deferred royalties	22	142
Total Deferred Revenue	<u>2,636</u>	<u>3,033</u>
Less long-term amounts:		
Deferred royalties	11	23
Total Deferred Revenue - Long-Term	<u>11</u>	<u>23</u>
Total Deferred Revenue - Current	<u>\$ 2,625</u>	<u>\$ 3,010</u>

NOTE 4 — INTANGIBLE ASSETS AND GOODWILL

The Company conducted its annual impairment test of goodwill as of June 30, 2017 and determined that there was no impairment. The Company also tests its intangible assets and goodwill between the annual impairment test if events occur or circumstances change that would more likely than not reduce the fair value of the Company or its assets below their carrying amounts. For intangible assets subject to amortization, the Company performs its impairment test when indicators, such as reductions in demand or significant economic slowdowns, are present. No events have occurred that triggered further impairment testing of the Company's intangible assets and goodwill during the years ended December 31, 2017 and 2016.

As of December 31, 2017 and December 31, 2016, the Company had goodwill (indefinite life) of \$2.9 million. As of December 31, 2017 and December 31, 2016, all intangible assets have been fully amortized. There was no amortization expense for the year ended December 31, 2017. Amortization expense for the years ended December 31, 2016 and 2015 totaled \$51,000 and \$63,000, respectively.

The following table presents the details of the Company's intangible assets, related accumulated amortization and goodwill (in thousands):

	As of December 31, 2017 and 2016			
	Gross	Accumulated Amortization	Impairment	Carrying Value
Patents (4-10 years)	\$ 1,914	\$ (1,914)	\$ —	\$ —
Trademarks (6 years)	69	(69)	—	—
Other (4 to 6 years)	817	(817)	—	—
Total	\$ 2,800	\$ (2,800)	\$ —	\$ —
Goodwill (Indefinite life)	\$ 2,926			\$ 2,926

NOTE 5 — INCOME TAXES

The Company accounts for income taxes under the asset and liability method, whereby deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Management evaluates the need to establish a valuation allowance for deferred tax assets based upon the amount of existing temporary differences, the period in which they are expected to be recovered, and expected levels of taxable income. A valuation allowance to reduce deferred tax assets is established when it is "more likely than not" that some or all of the deferred tax assets will not be realized. Management has determined that a full valuation allowance against the Company's net deferred tax assets is appropriate.

The following table presents the current and deferred provision for income taxes for the years ended December 31 (in thousands):

	2017	2016	2015
Current:			
Federal	\$ —	\$ —	\$ —
State	19	22	30
Foreign	93	69	87
	<u>112</u>	<u>91</u>	<u>117</u>
Deferred:			
Federal	(694)	60	61
State	—	—	—
Foreign	—	—	—
	<u>(694)</u>	<u>60</u>	<u>61</u>
	<u>\$ (582)</u>	<u>\$ 151</u>	<u>\$ 178</u>

The provision for income taxes differs from the amount that would result from applying the federal statutory rate as follows for the years ended December 31:

	2017	2016	2015
Statutory regular federal income tax rate	(34.0)%	(34.0)%	(34.0)%
Change in valuation allowance	(90.6)%	40.4 %	40.2 %
State tax benefit (net of federal benefit)	(3.2)%	(3.0)%	(3.1)%
Research credits	(1.7)%	(3.4)%	(3.1)%
Foreign amounts with no tax benefit	— %	0.2 %	0.1 %
Non-deductible expenses	1.0 %	0.6 %	0.4 %
Effect of change in rate from federal Tax Reform	127.1 %	0.5 %	0.9 %
Other	(2.0)%	(0.2)%	(0.5)%
Total	<u>(3.4)%</u>	<u>1.1 %</u>	<u>0.9 %</u>

The components of the deferred income tax assets and liabilities as of December 31 (in thousands):

	2017	2016
Capitalized intangible assets for tax purposes	\$ (21)	\$ 47
Reserves not currently deductible	1,130	2,117
Deferred revenue	5	8
Stock options	3,600	4,966
State taxes	6	9
Income tax credits	2,640	2,379
Inventory	495	940
Property and equipment	165	201
Other comprehensive income	—	252
Unrealized gain on foreign currency	84	136
Net operating losses	33,451	43,687
Total deferred tax assets	41,555	54,742
Valuation allowance	(40,866)	(54,310)
Net deferred tax assets	689	432
Capitalized intangible assets	(608)	(876)
Other	(185)	(354)
Total deferred tax liabilities	(793)	(1,230)
Net deferred tax liabilities	\$ (104)	\$ (798)

Based upon the Company's operating losses incurred for each of three years ended December 31, 2017, and the available evidence, the Company has established a valuation allowance against its net deferred tax assets in the amount of \$40.9 million as of December 31, 2017. Management considered factors such as the Company's earnings history, future projected earnings, and tax planning strategies. If sufficient evidence of the Company's ability to generate sufficient future taxable income tax benefits becomes apparent, the valuation allowance may be reduced, thereby resulting in tax benefits in the statement of operations and additional paid-in-capital. Management evaluates the potential realization of the Company's deferred tax assets and assesses the need for reducing the valuation allowance periodically.

The reversal of valuation allowance is primarily due to reduction in corporate income tax rate resulting from enactment of Tax Cuts and Jobs Act further discussed below.

As of December 31, 2017, the Company had net operating loss ("NOL") carryforwards for federal and state purposes of approximately \$147.0 million and \$87.0 million, respectively, which expire in 2018 through 2037. The utilization of NOL and credit carryforwards may be limited under the provisions of the Internal Revenue Code ("IRC") Section 382 and similar state provisions. IRC Section 382 generally imposes an annual limitation on the amount of NOL carryforwards that may be used to offset taxable income where a corporation has undergone significant changes in stock ownership. As of December 31, 2017, the Company had research and development tax credit carryforwards for federal and state purposes of approximately \$1.4 million and \$1.8 million, respectively, which will begin to expire in 2018 through 2037 for federal purposes and will carry forward indefinitely for state purposes. An updated analysis may be required at the time the Company begins utilizing any of its net operating losses to determine if there is an IRC Section 382 limitation.

The following table summarizes the activity related to the Company's unrecognized tax benefits during the year ended December 31, 2017 (in thousands):

Balance at January 1, 2017	\$ 568
Additions for tax positions related to the prior year	—
Lapse of statute of limitations	—
Balance at December 31, 2017	\$ 568

The Company expects resolution of unrecognized tax benefits, if created, would occur while the full valuation allowance of deferred tax assets is maintained. The Company does not expect to have any unrecognized tax benefits that, if recognized, would affect the effective tax rate. As of December 31, 2017 and 2016, the Company does not have liability for potential penalties or interest. The Company does not expect its unrecognized tax benefits to change significantly over the next 12 months.

The Company files U.S., state and foreign income tax returns in jurisdictions with varying statutes of limitations. The 2013 through 2017 tax years generally remain subject to examination by federal and most state tax authorities. In foreign jurisdictions, the 2011 through 2017 tax years remain subject to examination by their respective tax authorities.

On December 22, 2017, the U.S. federal government enacted the Tax Cuts and Jobs Act (the “2017 Tax Act”). Management reviewed and incorporated the new tax bill implications in the 2017 financial statements. The main change is the remeasurement of deferred taxes at the new corporate tax rate of 21%, which reduced the Company’s net deferred tax assets, before valuation allowance, by \$21.7 million. Due to full valuation allowance, the change in deferred taxes was fully offset by the change in valuation allowance other than deferred tax liability recorded against indefinite-lived intangible asset. The net impact of change in federal corporate rate against this deferred tax liability was \$0.3 million. In addition and consistent with the 2017 Tax Act, net operating losses generated subsequent to December 31, 2017 have an indefinite carryforward period with a limitation on utilization of 80% of taxable income in any given year. Therefore, to the extent that deductible temporary differences are expected to reverse and generate an indefinite-lived net operating loss, such assets are available to offset the naked credit deferred tax liability balance up to 80%. Accordingly, the Company recorded a reduction in its deferred tax liability balance from \$0.5 million to \$0.1 million and recognized a corresponding deferred tax benefit of \$0.4 million.

U.S. income taxes or withholding taxes were provided for all the distributed earnings for the Company’s foreign subsidiaries as of December 31, 2017. At December 31, 2017, unremitted earnings of foreign subsidiaries were approximately \$0.6 million and have been included in our computation of the transition tax associated with the enactment of the 2017 Tax Act discussed above. We do not provide for U.S. taxes on our unremitted earnings of foreign subsidiaries that have not been previously taxed since we intend to invest such undistributed earnings indefinitely outside of the U.S.

NOTE 6 — COMMITMENTS AND CONTINGENCIES

Leases

The Company leases its 57,000 square foot corporate headquarters and manufacturing facility located at 4 Cromwell, Irvine, California. In March 2015, the corporate headquarters and manufacturing facility lease was amended to extend the term through April 30, 2020, modify provisions for tenant improvement allowance of up to \$398,000, and adjust the basic rent terms. Future minimum rental commitments under operating lease agreements with non-cancelable terms greater than one year for the years ending December 31 are listed below. The Company also leases additional office space and certain office equipment under various operating lease arrangements.

In February 2015, the Company entered into a 30-month capital lease agreement for information technology equipment. Future minimum lease payments (using a 1.6% interest rate) under the capital lease, together with the present value of the net minimum lease payments and net of a \$14,000 prepayment, for the year ending December 31, 2018 is zero. The current obligation with respect to the present value of net minimum lease payments is reflected in the Consolidated Balance Sheets classified as an accrued liability, and there was no remaining portion of the present value of net minimum lease payments classified as a long-term obligation within capital lease obligations as of December 31, 2017. In February 2018, the Company extended the agreement for information technology equipment for an additional lease term of 18 months. In accordance with relevant accounting guidance, the renewal of this lease constituted a new lease and is classified by the Company as an operating lease.

Future minimum rental commitments under lease agreements, including both operating and capital leases as of December 31, 2017, with non-cancelable terms greater than one year for each of the years ending December 31 are as follows (in thousands):

2018	\$	814
2019		744
2020		283
2021		12
Thereafter		—
Total future minimum lease obligations	\$	<u>1,853</u>

Rent expense totaled approximately \$1.0 million for each of the years ended December 31, 2017, 2016, and 2015.

Employee Arrangements and Other Compensation

Certain members of management are entitled to severance benefits payable upon termination following a change in control, which would approximate \$1.7 million and \$1.3 million at December 31, 2017 and 2016, respectively. The Company also has agreements with certain employees to pay bonuses based on targeted performance criteria. As of December 31, 2017 and 2016, approximately \$67,000 and \$67,000 was accrued for performance bonuses, which is included in accrued liabilities in the Consolidated Balance Sheets.

Purchase Commitments

The Company generally purchases components and subassemblies for its products from a limited group of third-party suppliers through purchase orders. The Company had \$10.3 million of purchase commitments as of December 31, 2017, for which the Company has not received the goods or services and which is expected to be purchased primarily within one year. These purchase commitments were made to secure better pricing and to ensure the Company will have the necessary parts to meet anticipated near term demand. Although open purchase orders are considered enforceable and legally binding, the Company may be able to cancel, reschedule, or adjust requirements prior to supplier fulfillment.

Litigation

The Company discloses material loss contingencies deemed to be reasonably possible and accrues for loss contingencies when, in consultation with its legal advisors, management concludes that a loss is probable and reasonably estimable. The ability to predict the ultimate outcome of such matters involves judgments, estimates, and inherent uncertainties. The actual outcome of such matters could differ materially from management's estimates.

Intellectual Property Litigation

On April 24, 2012, CAO Group, Inc. ("CAO") filed a lawsuit against BIOLASE in the District of Utah alleging that BIOLASE's ezlase dental laser infringes on U.S. Patent No. 7,485,116 (the "116 Patent"). On September 9, 2012, CAO amended its complaint, adding claims for (1) business disparagement/injurious falsehood under common law and (2) unfair competition under 15 U.S.C. Section 1125(a). The additional claims stem from a press release that BIOLASE issued on April 30, 2012, which CAO claims contained false statements that are disparaging to CAO and its diode product. The amended complaint seeks injunctive relief, treble damages, attorneys' fees, punitive damages, and interest. Until January 24, 2018, this lawsuit was stayed in connection with United States Patent and Trademark Office proceedings relating to the 116 Patent, which proceedings ultimately culminated in a January 27, 2017 decision by the United States Court of Appeals for the Federal Circuit, affirming the findings of the Patent Trial and Appeal Board, which were generally favorable to the Company. On January 25, 2018, CAO moved for leave to file a second amended complaint to add certain claims, which filing the Company is not opposing.

On January 23, 2018, CAO filed a lawsuit against BIOLASE in the Central District of California alleging that BIOLASE's diode lasers infringe on U.S. Patent Nos. 8,337,097, 8,834,497, 8,961,040 and 8,967,883. The complaint seeks injunctive relief, treble damages, attorneys' fees, punitive damages, and interest.

NOTE 7 — STOCKHOLDERS' EQUITY

Preferred Stock

The BIOLASE board of directors (the "Board"), without further stockholder authorization, may issue from time to time up to 1,000,000 shares of the Company's preferred stock. Of the 1,000,000 shares of preferred stock, 500,000 shares are designated as Series B Junior Participating Cumulative Preferred Stock. As of December 31, 2017 and 2016, no preferred stock was issued. As of December 31, 2017 and 2016, no preferred stock was outstanding.

Common Stock

At December 31, 2017, the Company had 102,339,682 shares of BIOLASE common stock issued and outstanding. BIOLASE currently has 200,000,000 shares of Company common stock authorized for issuance.

2017 Common Stock Issuances

Rights Offering. The Company completed a rights offering on December 5, 2017 by selling 26,302,703 shares of common stock. Gross proceeds were approximately \$12.0 million, and net proceeds, after offering expenses of approximately \$0.6 million, were approximately \$11.4 million. Certain affiliates of Larry Feinberg and an affiliate of Jack Schuler exercised their basic subscription rights and over-subscription privilege in the rights offering and purchased a total of 10,745,614 shares and 10,964,912 shares of our common stock, respectively, on the same terms as all other participants. The Company plans to use the net proceeds from the rights offering for general working capital needs.

Private Placement. The Company completed a private placement on April 18, 2017. For information regarding this private placement, see *Note 1-Convertible Preferred Stock and Warrant Transactions*.

2016 Common Stock Issuance

Private Placement. The Company completed a private placement on August 8, 2016. For information regarding this private placement, see *Note 1-Convertible Preferred Stock and Warrant Transactions*.

Stock Dividends

There were no dividends paid or declared in 2017, 2016 or 2015.

Warrants

BIOLASE issues warrants for the sale of its common stock as approved by its Board. Warrants to purchase up to an aggregate of 3,925,871 unregistered shares of BIOLASE common stock at an exercise price of \$1.80 per share were issued in connection with the Company's April 2017 private placement. Warrants to purchase up to an aggregate of 2,035,398 unregistered shares of BIOLASE common stock at an exercise price of \$2.00 per share were issued in connection with the Company's August 2016 private placement. Both private placements are accounted for within stockholders' equity on the Consolidated Balance Sheets in accordance with GAAP.

The following table summarizes warrant activity (in thousands, except per share data):

	Shares	Weighted-Average Exercise Price Per Share
Warrants outstanding, January 1, 2015	10,094	\$ 4.18
Granted/Issued	—	\$ —
Exercised	—	\$ —
Forfeited, cancelled, or expired	—	\$ —
Warrants outstanding, December 31, 2015	10,094	\$ 4.18
Granted/Issued	2,035	\$ 2.00
Exercised	—	\$ —
Forfeited, cancelled, or expired	(723)	\$ 6.50
Warrants outstanding, December 31, 2016	11,406	\$ 4.18
Granted/Issued	3,926	\$ 1.80
Exercised	—	\$ —
Forfeited, cancelled, or expired	(9,206)	\$ 4.00
Warrants outstanding, December 31, 2017	6,126	\$ 1.93
Warrants exercisable, December 31, 2017	5,991	\$ 1.88
Vested warrants expired during the 12 months ended December 31, 2017	9,206	\$ 4.00

Stock Options

The Company currently has one stock-based compensation plan, the 2002 Stock Incentive Plan (as amended effective as of May 26, 2004, November 15, 2005, May 16, 2007, May 5, 2011, June 6, 2013, August 27, 2014, April 27, 2015 and May 6, 2016) (the "2002 Plan"), which will expire on May 5, 2019. Persons eligible to receive awards under the 2002 Plan include officers and employees of the Company, directors of the Company, and consultants. As of December 31, 2017, a total of 15,550,000 shares have been authorized for issuance under the 2002 Plan, of which 3,963,696 shares of BIOLASE common stock have been issued pursuant to options that were exercised, 8,526,388 shares of BIOLASE common stock have been reserved for options and restricted stock units that are outstanding, and 3,059,916 shares of BIOLASE common stock remain available for future grants.

Stock options may be granted as incentive or non-qualified options; however, no incentive stock options have been granted to date. The exercise price of options is at least equal to the market price of the stock as of the date of grant. Options may vest over various periods but typically vest on a quarterly basis over four years. Options expire after five years, ten years, or within a specified time from termination of employment, if earlier. The Company issues new shares of BIOLASE common stock upon the exercise of stock options. The following table summarizes option activity under the 2002 Plan (in thousands, except per share data):

	Shares	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value(1)
Options outstanding, January 1, 2015	3,475	\$ 3.03		
Granted at fair market value	1,931	\$ 2.22		
Granted at above fair market value	1,340	\$ 2.46		
Exercised	(38)	\$ 1.15		
Forfeited, cancelled, or expired	(2,215)	\$ 2.64		
Options outstanding, December 31, 2015	4,493	\$ 3.03		
Granted at fair market value	3,113	\$ 1.42		
Exercised	(1)	\$ 0.82		
Forfeited, cancelled, or expired	(993)	\$ 3.01		
Options outstanding, December 31, 2016	6,612	\$ 2.72		
Granted at fair market value	2,231	\$ 1.03		
Exercised	(3)	\$ 0.86		
Forfeited, cancelled, or expired	(2,103)	\$ 1.83		
Options outstanding, December 31, 2017	6,737	\$ 1.80	7.21	\$ —
Options exercisable, December 31, 2017	3,454	\$ 2.24	5.57	\$ —
Vested options expired during the 12 months ended December 31, 2017	288	\$ 3.42		

- (1) The intrinsic value calculation does not include negative values. This can occur when the fair market value on the reporting date is less than the exercise price of a grant.

The following table summarizes additional information for those options under the 2002 Plan that are outstanding and exercisable as of December 31, 2017 (in thousands, except per share data):

Range of Exercise Prices	Options Outstanding			Exercisable	
	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Life (Years)	Number of Shares	Weighted-Average Exercise Price
\$ 0.43 — \$ 1.21	1,428	\$ 0.80	8.65	451	\$ 0.97
\$ 1.22 — \$ 1.44	917	\$ 1.42	7.67	563	\$ 1.42
\$ 1.45 — \$ 1.60	1,481	\$ 1.48	8.93	3	\$ 1.45
\$ 1.61 — \$ 2.38	1,573	\$ 2.02	6.70	1,207	\$ 2.08
\$ 2.39 — \$ 5.07	1,338	\$ 3.20	4.06	1,230	\$ 3.25
Total	6,737	\$ 1.80	7.21	3,454	\$ 2.24

Cash proceeds, along with fair value disclosures related to grants, exercises, and vesting options, are as follows for the years ended December 31 (in thousands, except per share amounts):

	Years Ended December 31,		
	2017	2016	2015
Proceeds from stock options exercised	\$ 3	\$ 1	\$ 44
Tax benefit related to stock options exercised(1)	N/A	N/A	N/A
Intrinsic value of stock options exercised(2)	\$ 1	\$ —	\$ 52
Weighted-average fair value of options granted	\$ 0.69	\$ 1.03	\$ 1.54
Total fair value of shares vested during the year	\$ 1,286	\$ 1,728	\$ 2,268

- (1) Excess tax benefits received related to stock option exercises are presented as financing cash inflows. For the periods presented, the Company did not receive a tax benefit related to the exercise of stock options due to its net operating losses.
- (2) The intrinsic value of stock options exercised is the amount by which the market price of the stock on the date of exercise exceeded the market price of the stock on the date of grant.

2017 Stock Option Activity

Effective February 6, 2017, the Compensation Committee of the Board issued 611,000 non-qualified stock options to purchase shares of BIOLASE common stock to certain employees of the Company. These awards were issued at \$1.55 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. Vesting periods for options are as follows: (i) for the 586,000 options awarded to existing employees, one-half vest on the first anniversary of grant date and one-half vest on the second anniversary of the grant date and (ii) for the 25,000 options awarded to new employees, 25% vest on February 6, 2018 and the remainder vest ratably over the 36-month period, commencing on March 6, 2018.

On May 10, 2017, non-employee directors of the Company were granted a total of 525,528 non-qualified stock options to purchase shares of BIOLASE common stock. These awards were issued at \$1.21 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. The total grant vests in equal installments over a consecutive 12-month period, commencing on June 10, 2017.

On September 1, 2017, Paul N. Clark resigned from the Board, effective September 11, 2017, and as Chairman of the Board, effective September 1, 2017. Effective September 1, 2017, Dr. Jonathan T. Lord was appointed Chairman of the Board. On September 11, 2017, the Compensation Committee of the Board approved a modification to expiration dates applicable to Mr. Clark's vested options. As a result of the modification, the Company recognized additional compensation expense of \$44,000 for the year ended December 31, 2017. On September 11, 2017, Dr. Lord was granted 65,385 non-qualified stock options to purchase shares of BIOLASE common stock at \$0.54 per share, the closing market price of BIOLASE common stock on the grant date, and expiring 10 years from the grant date. On September 12, 2017, Dr. Lord was granted 65,891 non-qualified stock options to purchase shares of BIOLASE common stock at \$0.61 per share, the closing market price of BIOLASE common stock on the grant date, and expiring 10 years from the grant date. Both grants vest in equal installments over an eight-month period, commencing on October 10, 2017.

On October 27, 2017, Frederic H. Moll, M.D. resigned from the Board, effective November 11, 2017. On November 11, 2017, the Compensation Committee of the Board approved a modification to expiration dates applicable to Dr. Moll's vested options. As a result of the modification, the Company recognized additional compensation expense of \$22,000 for the year ended December 31, 2017. Also on October 27, 2017, the Board elected Richard B. Lanman, M.D. to the Board. In connection with his election to the Board, on November 1, 2017, Dr. Lanman was granted 135,333 non-qualified stock options to purchase shares of BIOLASE common stock at \$0.75 per share, the closing market price of BIOLASE common stock on the grant date, and expiring 10 years from the grant date.

Effective November 7, 2017, the Compensation Committee of the BIOLASE board of directors issued 426,000 non-qualified stock options to purchase shares of BIOLASE common stock to certain employees of the Company. These awards were issued at \$0.60 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. Vesting periods for options are as follows: one-half vest on the first anniversary of the grant date and one-half vest ratably monthly commencing thirteen months after the grant date through the twenty-fourth month.

2016 Stock Option Activity

On February 26, 2016, the Compensation Committee of the Board awarded to certain employees and consultants of the Company a total of 295,000 non-qualified stock options to purchase shares of BIOLASE common stock. These awards were issued at \$0.86 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. Vesting periods for options are as follows: (i) 185,000 options, awarded to existing employees, vest ratably over a 48 month period, commencing one month from the grant date, and (ii) 110,000 options, awarded to new 2016 employees, vest 25% on the one-year anniversary of the grant date and the remainder ratably over the 36-month period, commencing 13 months after of the grant date.

On April 18, 2016, in connection with the hiring of the two new Vice Presidents, the Compensation Committee of the Board awarded 325,000 non-qualified stock options to purchase shares of BIOLASE common stock. These awards were issued at \$1.43 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. Vesting periods for the options are as follows: (i) one-half of the total grant is subject to time vesting, with 25% vesting as of April 18, 2017 and the remaining 75% vesting ratably monthly over a 36-month period commencing on April 18, 2017, and (ii) one-half of the total grant is subject to specific 2016 and 2017 performance criteria, with vesting upon completion of the applicable performance criteria. As of December 31, 2016, 243,750 non-qualified stock options to purchase shares of BIOLASE common stock remain outstanding.

On May 6, 2016, non-employee directors of the Company were granted a total of 597,757 non-qualified stock options to purchase shares of BIOLASE common stock. These awards were issued at \$1.41 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. The total grant vests in equal installments over a consecutive 12-month period, commencing on June 6, 2016.

On August 29, 2016, in connection with the hiring of a new Senior Director, the Compensation Committee of the Board awarded 60,000 non-qualified stock options to purchase shares of BIOLASE common stock. This award was issued at \$1.65 per share, the closing market price of BIOLASE common stock on the grant date, and expires 10 years from the grant date. Vesting periods for the options are as follows: (i) one-half of the total grant is subject to ratable time vesting over a 48-month period commencing on September 29, 2016, and (ii) one-half of the total grant is subject to specific 2017 performance criteria, with vesting upon completion of the applicable performance criteria. As of December 31, 2016, 60,000 non-qualified stock options to purchase shares of BIOLASE common stock remain outstanding.

On September 15, 2016, in connection with the hiring of a new Vice President, the Compensation Committee of the Board awarded 250,000 non-qualified stock options to purchase shares of BIOLASE common stock. This award was issued at \$1.78 per share, the closing market price of BIOLASE common stock on the grant date, and expires 10 years from the grant date. Vesting periods for the options are as follows: (i) one-half of the total grant is subject to time vesting with 25% vesting as of September 15, 2017 and the remaining 75% vesting ratably monthly over a 36-month period commencing on September 15, 2017, and (ii) one-half of the total grant is subject to specific 2017 and 2018 performance criteria, with vesting upon completion of the applicable performance criteria. As of December 31, 2016, 250,000 non-qualified stock options to purchase shares of BIOLASE common stock remain outstanding.

On October 3, 2016, in connection with the hiring of a new Vice President, the Compensation Committee of the Board awarded 125,000 non-qualified stock options to purchase shares of BIOLASE common stock. This award was issued at \$1.72 per share, the closing market price of BIOLASE common stock on the grant date, and expires 10 years from the grant date. Vesting periods for the options are as follows: (i) one-half of the total grant is subject to time vesting with 25% vesting as of October 3, 2017 and the remaining 75% vesting ratably monthly over a 36-month period commencing on October 3, 2017, and (ii) one-half of the total grant is subject to specific 2017 through 2019 performance criteria, with vesting upon completion of the applicable performance criteria. As of December 31, 2016, 125,000 non-qualified stock options to purchase shares of BIOLASE common stock remain outstanding.

During the year ended December 31, 2016, the Compensation Committee of the Board granted non-qualified stock options to purchase 1.4 million shares of BIOLASE common stock to the Company's President and Chief Executive Officer. The exercise price of such options ranged from \$1.44-\$1.45 per share, vest over two to four years, and expire 10 years from the grant date.

2015 Stock Option Activity

On January 2, 2015, the Compensation Committee of the Board granted non-qualified stock options to purchase 1,365,702 shares of BIOLASE common stock to certain officers of the Company in connection with a compensation plan for 2015 and 86,000 shares of BIOLASE common stock to members of the Dental Professional Advisory Board (“DPAB”) as consultants for the Company. These options were granted at an exercise price of \$2.64, the closing market price of BIOLASE common stock on the grant date. Options granted to certain officers of the Company expire ten years from the grant date and vest as follows: (i) as to 50% of the options, one-fourth on the one year anniversary of the grant date and the remaining three-fourths, ratably over the next 36 month period, commencing on the thirteenth month from grant date over a requisite service period of four years, and (ii) as to 50% of the options, upon achievement of specific annual Company performance criteria with a requisite service period of one year. Options granted to the DPAB fully vest and become exercisable upon the achievement of specified performance conditions, as defined in the consulting agreements, and expires five years from grant date.

On August 12, 2015, the Compensation Committee of the Board approved a modification to the performance criteria applicable to the unvested options. As a result of this modification, the fair value of the awards decreased by \$661,000, and the Company recognized additional compensation expense of \$154,000 for the year ended December 31, 2015. The vesting schedule and requisite service period of the award remained unchanged by the modification.

On December 31, 2015 the performance criteria related to the officer grants on January 2, 2015 was partially achieved and 80% of the performance-based options vested on January 2, 2016. As a result, 122,038 shares became available under the 2002 Plan on December 31, 2015, and options to purchase 488,170 shares vested on January 2, 2016.

Restricted Stock Units

2017 Restricted Stock Units Activity

Effective February 6, 2017, the Compensation Committee of the Board approved the grant of the following awards:

- 80,000 restricted stock units (“RSUs”) were awarded to an employee of the Company as part of the employee’s 2017 compensation. These awards were valued at \$1.55 per share, the closing market price of BIOLASE common stock on the grant date, and vest as follows: (i) 30,000 of the RSUs vested on March 14, 2017, (ii) 20,000 of the RSUs vested on September 14, 2017, and (iii) 30,000 of the RSUs vest on May 10, 2018.
- 1,000,000 stock-settled RSUs were awarded to the Company’s President and Chief Executive Officer as part of his 2017 compensation. These RSUs were valued at \$1.55 per share, the closing market price of BIOLASE common stock on the grant date. These RSUs vest as follows: (i) one-quarter of the RSUs vest on February 6, 2019, (ii) one-eighth of the RSUs vest on February 6, 2020, (iii) one-eighth of the RSUs vest on February 6, 2021, and (iv) one-half of the RSUs vest upon the achievement of specific interim and annual Company performance criteria.

On May 9, 2017 and in connection with the Company’s 2017 compensation plan, 500,000 RSUs were awarded to certain employees and consultants of the Company. These awards were valued at \$1.22 per share, the closing market price of BIOLASE common stock on the grant date. The RSUs vest as follows: (i) one-half of the total grant is subject to time vesting with 50% vesting on May 9, 2018 and the remaining 50% vesting on May 9, 2019, and (ii) one-half of the total grant is subject to specific 2017 and 2018 performance criteria, with vesting upon satisfaction of the applicable performance criteria.

On May 10, 2017, non-employee directors of the Company were granted a total of 175,176 RSUs valued at \$1.21 per share, the closing market price of BIOLASE common stock on the grant date. These awards vest on May 10, 2018. On September 1, 2017, Paul N. Clark resigned from the Board, effective September 11, 2017, and as Chairman of the Board, effective September 1, 2017. On September 11, 2017, the Compensation Committee of the Board approved a modification to the vesting criteria applicable to Mr. Clark’s unvested RSUs. As a result of the modification, the Company recognized additional compensation expense of \$12,000 for the year ended December 31, 2017. On October 27, 2017, Frederic H. Moll, M.D. resigned from the Board, effective November 11, 2017. On November 11, 2017, the Compensation Committee of the Board approved a modification to the vesting criteria applicable to Dr. Moll’s unvested RSUs. As a result of the modification, the Company recognized additional compensation expense of \$10,000 for the year ended December 31, 2017.

2016 Restricted Stock Units Activity

Under the 2002 Plan, effective February 26, 2016, the Compensation Committee of the Board granted the following awards:

- 388,500 restricted stock units (“RSUs”) were awarded to certain employees and consultants of the Company. These awards were valued at \$0.86 per share, the closing market price of BIOLASE common stock on the grant date, and fully vested on July 1, 2016.
- 140,000 RSUs were awarded to certain employees and consultants of the Company as part of their compensation plan. These awards were valued at \$0.86 per share, the closing market price of BIOLASE common stock on the grant date, and vest 25% on each of the first, second, third, and fourth anniversaries of the grant date.
- In connection with the President and Chief Executive Officer’s employment agreement, the maximum performance bonus was awarded, consisting of (i) \$100,000 paid in cash during the nine months ended September 30, 2016, and (ii) the grant of 59,523 RSUs, valued at \$0.86 per share, the closing market price of BIOLASE common stock on the grant date. Half of these RSUs vested on March 30, 2016 and half of these RSUs vested on February 18, 2017.

On March 10, 2016, the Compensation Committee of the Board approved the grant of 70,000 RSUs to the Company’s Chief Financial Officer as part of his 2015 compensation. These awards were valued at \$1.23 per share, the closing market price of BIOLASE common stock on the grant date, and fully vested on July 1, 2016.

On May 6, 2016, as compensation for their service during the current year, non-employee directors of the Company were granted a total of 248,750 RSUs valued at \$1.41 per share, the closing market price of BIOLASE common stock on the grant date. These awards vest on May 6, 2017.

The following table summarize RSU activity under the 2002 Plan (in thousands):

	Shares
Unvested restricted stock units, January 1, 2015	37
Granted	—
Vested	(37)
Forfeited or cancelled	—
Unvested restricted stock units, December 31, 2015	—
Granted	907
Vested	(488)
Forfeited or cancelled	—
Unvested restricted stock units, December 31, 2016	419
Granted	2,351
Vested	(404)
Forfeited or cancelled	(577)
Unvested restricted stock units, December 31, 2017	1,789

Inducement Stock-Based Awards

2017 Inducement Activity

On March 13, 2017, and as amended on April 19, 2017, in connection with the hiring of a new Vice President of Sales, the Compensation Committee of the Board awarded non-qualified stock options to purchase 400,000 shares of BIOLASE common stock. This award was issued at \$1.17 per share, the closing market price of BIOLASE common stock on the grant date, and expires 10 years from the grant date. Vesting periods for the options are as follows: (i) two-fifths of the total grant is subject to time vesting with 25% vesting as of March 13, 2018 and the remaining 75% vesting ratably monthly over a 36-month period commencing on March 13, 2018, and (ii) three-fifths of the total grant is subject to specific 2017 and 2018 performance criteria, with vesting upon satisfaction of the applicable performance criteria. This award was forfeited upon the departure of the Vice President of Sales in November 2017.

On March 27, 2017, in connection with the hiring of a new Senior Vice President and Chief Financial Officer, the Compensation Committee of the Board awarded non-qualified stock options to purchase 600,000 shares of BIOLASE common stock. This award was issued at \$1.28 per share, the closing market price of BIOLASE common stock on the grant date, and expires

10 years from the grant date. Vesting periods for the options are as follows: (i) two-thirds of the total grant is subject to time vesting with 25% vesting as of March 27, 2018 and the remaining 75% vesting ratably monthly over a 36-month period commencing on March 27, 2018, and (ii) one-third of the total grant is subject to specific 2017 and 2018 performance criteria, with vesting upon satisfaction of the applicable performance criteria. This award was forfeited upon the departure of the Senior Vice President and Chief Financial Officer in May 2017.

On October 2, 2017, in connection with the hiring of a new Senior Vice President and Chief Financial Officer, the Compensation Committee of the Board awarded non-qualified stock options to purchase 600,000 shares of BIOLASE common stock. This award was issued at \$0.59 per share, the closing market price of BIOLASE common stock on the grant date, and expires 10 years from the grant date. Vesting periods for the options are as follows: (i) two-thirds of the total grant is subject to time vesting with 25% vesting as of October 2, 2018 and the remaining 75% vesting ratably monthly over a 36-month period commencing on October 2, 2018, and (ii) one-third of the total grant is subject to specific 2018 and 2019 performance criteria, with vesting upon satisfaction of the applicable performance criteria.

2015 Inducement Activity

Effective March 9, 2015, the Compensation Committee of the Board granted non-qualified stock options to purchase up to 871,710 shares of BIOLASE common stock to the Company's Chief Financial Officer in connection with his employment agreement with BIOLASE. These options were granted at an exercise price of \$1.99 per share, the closing price of BIOLASE common stock on the grant date. These options expire ten years from the grant date and vest in two tranches as follows: (i) as to options to purchase 523,026 shares (the "First Tranche"), options to purchase 130,757 shares vested and became exercisable on March 9, 2016, and options to purchase 10,896 shares vest and become exercisable each month following March 9, 2016 for a period of 35 consecutive months, and options to purchase 10,909 shares vest and become exercisable on March 9, 2019, and (ii) as to options to purchase 348,684 shares (the "Second Tranche"), all such shares vest and become exercisable on March 9, 2025 or based on the Company's achievement of certain enumerated financial performance targets or other milestones, at the discretion of the Compensation Committee of the Board. The fair value of the First Tranche of \$1.48 per share was estimated using the Black-Scholes option-pricing model with assumptions of 6.1 years for expected term, 88.79% volatility and 1.83% risk-free interest rate. The fair value of the Second Tranche of \$1.70 per share was estimated using the Black-Scholes option-pricing model with assumptions of 10.0 years for expected term, 87.87% volatility and 2.19% risk-free interest rate. On December 30, 2016, the Chief Financial Officer tendered his resignation and entered into a transition letter agreement with the Company. Pursuant to the transition letter agreement, modifications occurred to vest 294,205 unvested options and extend the exercise period of 623,026 vested stock options from 90 days to one year. As a result of these modifications, the Company recognized additional compensation expense of \$215,000 for the year ended December 31, 2016.

On June 23, 2015 the Board elected to accelerate options to purchase 100,000 shares in the Second Tranche of the Chief Financial Officer's award. As of December 31, 2016, 100,000 shares were vested and exercisable.

Effective July 13, 2015, the Compensation Committee of the Board granted non-qualified stock options to purchase up to 870,000 shares of BIOLASE common stock to the Company's President and Chief Executive Officer in connection with his employment agreement with BIOLASE. These options were granted at an exercise price of \$1.64 per share, the closing price of BIOLASE common stock on the grant date. These options expire ten years from the grant date and vest over four years, with options to purchase 217,500 shares vesting and becoming exercisable on July 13, 2016 and options to purchase 18,125 shares vesting and becoming exercisable each month following July 13, 2016 for a period of 36 consecutive months.

Also effective July 13, 2015, the Compensation Committee of the Board awarded 870,000 stock-settled RSUs to its President and Chief Executive Officer in connection with his employment agreement with BIOLASE. The RSUs are valued at \$1.64 per share and vest upon the achievement of specific interim and annual Company performance criteria. As of December 31, 2016, 435,000 stock-settled RSUs remain outstanding.

NOTE 8 — SEGMENT INFORMATION

The Company currently operates in a single business segment. Management uses one measurement of profitability and does not segregate its business for internal reporting. Sales to customers located in the United States accounted for approximately 62%, 64%, and 61% of net revenue and international sales accounted for approximately 38%, 36%, and 39% of net revenue for the years ended December 31, 2017, 2016, and 2015, respectively. No individual international country represented more than 10% of net revenue during the years ended December 31, 2017, 2016, and 2015.

Net revenue by geographic location based on the location of customers was as follows (in thousands):

	Years Ended December 31,		
	2017	2016	2015
United States	\$ 29,296	\$ 33,385	\$ 29,433
International	17,630	18,425	19,042
	<u>\$ 46,926</u>	<u>\$ 51,810</u>	<u>\$ 48,475</u>

Long-lived assets by geographic location was as follows (in thousands):

	Years Ended December 31,		
	2017	2016	2015
United States	\$ 3,347	\$ 4,175	\$ 3,401
International	327	302	326
	<u>\$ 3,674</u>	<u>\$ 4,478</u>	<u>\$ 3,727</u>

NOTE 9 — CONCENTRATIONS

Revenue from the Company's products for the years ended December 31, 2017, 2016 and 2015 are as follows:

	Years Ended December 31,					
	2017		2016		2015	
Laser systems	29,121	62.0 %	35,150	67.9 %	32,691	67.5 %
Imaging systems	3,685	7.9 %	3,066	5.9 %	2,237	4.6 %
Consumables and other	7,332	15.6 %	6,906	13.3 %	6,877	14.2 %
Services	6,660	14.2 %	6,539	12.6 %	6,465	13.3 %
License fees and royalties	128	0.3 %	149	0.3 %	205	0.4 %
Total revenue	<u>46,926</u>	<u>100.0 %</u>	<u>51,810</u>	<u>100.0 %</u>	<u>48,475</u>	<u>100.0 %</u>

The Company maintains its cash and cash equivalent accounts with established commercial banks. Such cash deposits periodically exceed the Federal Deposit Insurance Corporation insured limit.

No individual customer represented more than 10% of the Company's accounts receivable at December 31, 2017 and 2016.

The Company currently purchases certain key components of its products from single suppliers. Although there are a limited number of manufacturers of these key components, management believes that other suppliers could provide similar key components on comparable terms. A change in suppliers, however, could cause delays in manufacturing and a possible loss of sales, which could adversely affect the Company's business, results of operations and financial condition.

NOTE 10 — SUBSEQUENT EVENTS (unaudited)

Lines of Credit

On March 6, 2018, BIOLASE and two of its wholly-owned subsidiaries (such subsidiaries, together with BIOLASE, the "Borrower") entered into a Business Financing Agreement (the "Business Financing Agreement"). Pursuant to the terms and conditions of the Business Financing Agreement, Western Alliance has agreed to provide the Borrower a secured revolving line of credit permitting the Borrower to borrow or receive letters of credit up to the lesser of \$6.0 million (subject to a \$6.0 million credit limit relating to domestic eligible accounts receivable (the "domestic credit limit") and a \$3.0 million credit limit relating to export-related eligible accounts receivable (the "EXIM credit limit")) and the borrowing base, which is defined as the sum of the domestic borrowing base (up to 75.0% of the Borrower's eligible domestic accounts receivable less such reserves as Western Alliance may deem proper and necessary) and the export-related borrowing base (up to 85.0% of the Borrower's eligible export-related accounts receivable less such reserves as Western Alliance may deem proper and necessary). The Business Financing Agreement expires on March 6, 2020, and the Borrower's obligations thereunder are secured by a security interest in all of the Borrower's assets.

Amounts outstanding under the Business Financing Agreement bear interest at a per annum floating rate equal to the greater of 4.5% or the “Prime Rate” published in the Money Rates section of the Western Edition of The Wall Street Journal (or such other rate of interest publicly announced from time to time by Western Alliance as its “Prime Rate”), plus 1.5% with respect to advances made under the line of credit, plus an additional 5.0% during any period that an event of default has occurred and is continuing. The commitment fee under the Business Financing Agreement is 0.25% of the domestic credit limit and 1.75% of the EXIM credit limit and is payable on March 6, 2018 and each anniversary thereof.

Warrant Issuance

On March 6, 2018, in connection with the Business Financing Agreement, BIOLASE issued to Western Alliance a warrant (the “Western Alliance Warrant”) to purchase a number of shares of BIOLASE common stock equal to \$120,000 divided by the exercise price of \$0.47 (as adjusted), which was the closing price of BIOLASE common stock on the Nasdaq Capital Market on March 6, 2018. The Western Alliance Warrant is immediately exercisable and expires on March 6, 2028.

Equity Awards

Stock Options

Effective January 25, 2018, the Compensation Committee of the Board issued 1.8 million non-qualified stock options to purchase shares of BIOLASE common stock were awarded to certain employees of the Company. These awards were valued at \$0.42 per share, the closing market price of BIOLASE common stock on the grant date, and expire 10 years from the grant date. Vesting periods for options is ratably over the 36-month period, commencing on February 25, 2018.

Restricted Stock Units

Effective January 26, 2018, the Board issued 200,000 RSUs to the Company’s President and Chief Executive Officer. This award was valued at \$0.40 per share, the closing market price of BIOLASE common stock on the grant date, and will vest upon the achievement of specific annual Company performance criteria.

Further discussion of the stock-based compensation is discussed in *Note 7 – Stockholders’ Equity*.

BIOLASE, INC.

**Schedule II — Consolidated Valuation and Qualifying Accounts and Reserves
For the Years Ended December 31, 2017, 2016, and 2015
(in thousands)**

	Balance at Beginning of Year	Charges (Reversals) to Cost or Expenses	Deductions	Balance at End of Year
Year Ended December 31, 2017:				
Allowance for doubtful accounts	\$ 1,209	\$ (401)	\$ (6)	\$ 802
Allowance for sales returns	210	—	—	210
Allowance for tax valuation	54,310	(13,444)	—	40,866
Year Ended December 31, 2016:				
Allowance for doubtful accounts	\$ 1,765	\$ (438)	\$ (118)	\$ 1,209
Allowance for sales returns	210	—	—	210
Allowance for tax valuation	49,514	4,796	—	54,310
Year Ended December 31, 2015:				
Allowance for doubtful accounts	\$ 1,711	\$ 86	\$ (32)	\$ 1,765
Allowance for sales returns	110	100	—	210
Allowance for tax valuation	42,069	7,445	—	49,514

THIS WARRANT AND THE SHARES ISSUABLE HEREUNDER HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE “ACT”), AND MAY NOT BE SOLD, PLEDGED, OR OTHERWISE TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION THEREOF UNDER SUCH ACT OR PURSUANT TO RULE 144 OR AN OPINION OF COUNSEL REASONABLY SATISFACTORY TO THE COMPANY AND ITS COUNSEL, THAT SUCH REGISTRATION IS NOT REQUIRED.

WARRANT TO PURCHASE STOCK

Issuer: BIOLASE, INC., a Delaware corporation (the “Company”)

Number of Shares: the number of fully paid and non-assessable shares (after taking into account adjustments made pursuant to stock splits, reverse stock splits and other events specified in Article 2) of Common Stock obtained by dividing (i) \$120,000, by (ii) the applicable Exercise Price at the time this Warrant is exercised.

Class of Stock: Common Stock

Exercise Price per Share: \$0.4656 (as may be adjusted in accordance with Article 2)

Issue Date: March 6, 2018

Expiration Date: March 6, 2028

THIS WARRANT CERTIFIES THAT, for the agreed upon value of \$1.00 and for other good and valuable consideration, WESTERN ALLIANCE BANK, or its assignees (“Holder”) is entitled to purchase the number of fully paid and nonassessable shares of the Company’s capital stock set forth above (the “Shares”) at the Exercise Price per Share set forth above, as the same may be from time to time adjusted pursuant to Article 2 hereof and subject to the provisions and upon the terms and conditions set forth in this Warrant.

ARTICLE 1 EXERCISE.

1.1 Method of Exercise. This Warrant is exercisable, in whole or in part, at any time and from time to time on or before the Expiration Date set forth above. Holder may exercise this Warrant by delivering a duly executed Notice of Exercise, in substantially the form attached hereto as Appendix 1, to the principal office of Company. Unless Holder is exercising the conversion right set forth in Section 1.2, Holder shall also deliver to Company an amount equal to the aggregate Exercise Price for Shares being purchased, by check or wire.

1.2 Conversion Right. In lieu of exercising this Warrant as specified in Section 1.1, Holder may from time to time convert this Warrant, in whole or in part, into a number of Shares determined by dividing (a) the aggregate fair market value of Shares or other securities otherwise issuable upon exercise of this Warrant minus the aggregate Exercise Price of such Shares by (b) the fair market value of one Share. The fair market value of Shares shall be determined pursuant to Section 1.3.

1.3 Fair Market Value. If the Shares are traded in a public market, the fair market value of the Shares shall be the closing price of the Shares (or the closing price of the Company’s stock into which the Shares are convertible) reported for the business day immediately before Holder

delivers its Notice of Exercise to the Company. If the Shares are not traded in a public market, the Board of Directors of Company shall determine fair market value in its reasonable good faith judgment. The foregoing notwithstanding, if Holder advises the Board of Directors in writing that Holder disagrees with such determination, then Company and Holder shall promptly agree upon a reputable investment banking firm to undertake such valuation. If the valuation of such investment banking firm is greater than that determined by the Board of Directors, then all fees and expenses of such investment banking firm shall be paid by Company. In all other circumstances, such fees and expenses of such investment banking firm shall be paid by Holder.

1.4 Delivery of Certificate and New Warrant. Promptly (and in no event more than 3 business days after exercise) after Holder exercises or converts this Warrant, Company shall deliver to Holder certificates for Shares acquired and, if this Warrant has not been fully exercised or converted and has not expired, a new Warrant representing Shares not yet acquired.

1.5 Replacement of Warrant. On receipt of evidence reasonably satisfactory to Company of the loss, theft, destruction or mutilation of this Warrant and, in the case of loss, theft or destruction, on delivery of an indemnity agreement reasonably satisfactory in form and amount to Company or, in the case of mutilation, on surrender and cancellation of this Warrant, Company at its expense shall execute and deliver a replacement Warrant.

1.6 Sale, Merger, or Consolidation of Company. For the purpose of this Warrant, "Acquisition" means any sale, license, or other disposition of all or substantially all of the assets of Company, or any reorganization, consolidation, or merger of Company where the holders of Company's securities before the transaction beneficially own less than 50% of the outstanding voting securities of the surviving entity after the transaction. Upon the closing of any Acquisition, the successor entity shall assume the obligations of this Warrant, and this Warrant shall be exercisable for the same securities, cash, and property as would be payable for Shares issuable upon exercise of the unexercised portion of this Warrant as if such Shares were outstanding on the record date for the Acquisition and subsequent closing, and the Exercise Price shall be adjusted accordingly; provided that if pursuant to such Acquisition the entire outstanding class of Shares issuable upon exercise of the unexercised portion of this Warrant are cancelled and the total consideration payable to the holders of such class of Shares consists entirely of cash, then, upon payment to the holder of this Warrant of an amount equal to the amount such holder would receive if such holder held Shares issuable upon exercise of the unexercised portion of this Warrant and such Shares were outstanding on the record date for the Acquisition less the aggregate Exercise Price of such Shares, this Warrant shall be cancelled.

1.7 Automatic Cashless Exercise upon Expiration. In the event that, upon the Expiration Date or other termination of the warrant, the fair market value of one Share (or other security issuable upon the exercise hereof) as determined in accordance with Section 1.3 above is greater than the Exercise Price in effect on such date, then this Warrant shall automatically be deemed on and as of such date to be exercised pursuant to Section 1.2 above as to all Shares (or such other securities) for which it shall not previously have been exercised, and the Company shall, within a reasonable time, deliver a certificate representing the Shares (or such other securities) issued upon such exercise to Holder.

ARTICLE 2 ADJUSTMENTS.

2.1 Stock Dividends, Splits, Etc. If Company declares or pays a dividend on its common stock (or Shares, if Shares are securities other than common stock) payable in common stock or

other securities or property, subdivides the outstanding common stock into a greater amount of common stock, or, if Shares are securities other than common stock, subdivides Shares in a transaction that increases the amount of common stock into which Shares are convertible, then upon exercise of this Warrant, for each Share acquired, Holder shall receive, without cost to Holder, the total number and kind of securities to which Holder would have been entitled had Holder owned Shares on the record date the dividend or subdivision occurred since the original issue date of this Warrant.

2.2 Reclassification, Recapitalization, Exchange or Substitution. Upon any reclassification, recapitalization, exchange, substitution, or other event that results in a change of the number and/or class of the securities issuable upon exercise or conversion of this Warrant, Holder shall be entitled to receive, upon exercise or conversion of this Warrant, the number and kind of securities and property that Holder would have received for Shares if this Warrant had been exercised immediately before such reclassification, recapitalization, exchange, substitution, or other event. Company or its successor shall promptly issue to Holder a new Warrant for such new securities or other property. The new Warrant shall provide for adjustments which shall be as nearly equivalent as may be practicable to the adjustments provided for in this Article 2 including, without limitation, adjustments to the Exercise Price and to the number of securities or property issuable upon exercise of the new Warrant. The provisions of this Section 2.2 shall similarly apply to successive reclassifications, recapitalizations, exchanges, substitutions, or other events.

2.3 Adjustments for Combinations, Etc. If the outstanding Shares are combined or consolidated, by reclassification or otherwise, into a lesser number of shares, the Exercise Price shall be proportionately increased and the number of Shares as to which this warrant is exercisable shall be proportionately decreased.

2.4 Adjustments for Diluting Issuances. In the event of the issuance (a “Diluting Issuance”) by Company, after the Issue Date of the Warrant, of any Additional Shares of Common Stock (as defined in the Company’s Certificate of Incorporation) at a price per share less than the then Exercise Price, then the number of shares of common stock issuable upon conversion of the Shares, and the conversion price, shall be adjusted in accordance with those provisions (the “Provisions”) of Company’s Certificate of Incorporation which apply to Diluting Issuances with the same effect as though the shares were outstanding at the time of the diluting issuance. Company agrees that the Provisions, as in effect on the Issue Date, shall be deemed to remain in full force and effect during the term of the Warrant notwithstanding any subsequent amendment, waiver or termination thereof by Company’s shareholders. Under no circumstances shall the aggregate Exercise Price payable by Holder upon exercise of the Warrant increase as a result of any adjustment arising from a Diluting Issuance.

2.5 Reserved.

2.6 No Impairment. Company shall not, by amendment of its Certificate of Incorporation or through a reorganization, transfer of assets, consolidation, merger, dissolution, issue, or sale of securities or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms to be observed or performed under this Warrant by Company, but shall at all times in good faith assist in carrying out of all the provisions of this Article 2 and in taking all such action as may be necessary or appropriate to protect Holder’s rights under this Article against impairment. If Company takes any action affecting Shares or its common stock as described above

that adversely affects Holder's rights under this Warrant, the Exercise Price shall be adjusted downward and the number of Shares issuable upon exercise of this Warrant shall be adjusted upward in such a manner that such action is offset and the aggregate Exercise Price of this Warrant is unchanged.

2.7 Fractional Shares. No fractional Shares shall be issuable upon exercise or conversion of the Warrant and the number of Shares to be issued shall be rounded down to the nearest whole Share. If a fractional share interest arises upon any exercise or conversion of the Warrant, Company shall eliminate such fractional share interest by paying Holder an amount computed by multiplying the fractional interest by the fair market value of a full Share.

2.8 Certificate as to Adjustments. Upon each adjustment of the Exercise Price, Company at its expense shall promptly compute such adjustment, and furnish Holder with a certificate of its Chief Financial Officer setting forth the Exercise Price in effect upon the date thereof and the series of adjustments leading to such Exercise Price, and the facts upon which such adjustment is based.

ARTICLE 3 REPRESENTATIONS, WARRANTIES AND COVENANTS OF COMPANY.

3.1 Representations and Warranties. The Company hereby represents and warrants to Holder as follows:

(a) The initial Exercise Price referenced on the first page of this Warrant is not greater than the fair market value of the Shares as of the date of this Warrant.

(b) As of the date hereof, the Company has sufficient authorized shares reserved for the issuance of all capital stock which may be issued upon the exercise of this Warrant.

(c) The Company's capitalization table attached to this Warrant as Appendix 2 is true and complete as of the Issue Date.

3.2 Valid Issuance. Company shall take all steps necessary to insure that all Shares which may be issued upon the exercise of this Warrant, and all securities, if any, issuable upon conversion of Shares, shall, upon issuance, be duly authorized, validly issued, fully paid and nonassessable, and free of any liens and encumbrances except for restrictions on transfer provided for herein or under applicable federal and state securities laws.

3.3 Notice of Certain Events. If Company proposes at any time (a) to declare any dividend or distribution upon its common stock, whether in cash, property, stock, or other securities and whether or not a regular cash dividend; (b) to offer for subscription pro rata to the holders of any class or series of its stock any additional shares of stock of any class or series or other rights; (c) to effect any reclassification or recapitalization of common stock; (d) to merge or consolidate with or into any other corporation, or sell, lease, license, or convey all or substantially all of its assets, or to liquidate, dissolve or wind up; or (e) offer holders of registration rights the opportunity to participate in an underwritten public offering of the company's securities for cash, then, in connection with each such event, Company shall give Holder (1) in the case of the matters referred to in (a) and (b) above at least 20 days prior written notice of the date on which a record will be taken for such dividend, distribution, or subscription rights (and specifying the date on which the holders of common stock will be entitled thereto) or for determining rights to vote, if any, in respect of the matters referred to in (c) and (d) above; (2) in the case of the matters referred to in (c) and (d) above at least 20 days prior written notice of the date when the same will take place (and specifying the date on which the holders of common stock will be entitled to exchange their common stock for securities or other property deliverable upon the occurrence of such event); and

(3) in the case of the matter referred to in (e) above, the same notice as is given to the holders of such registration rights.

3.4 (a) Information. So long as Holder holds this Warrant and/or any of the Shares, Company shall deliver to Holder (i) promptly, copies of all notices or other written communications to which Holder would be entitled if it held Shares as to which this Warrant was then exercisable and (ii) such other financial statements required under and in accordance with any loan documents between Holder and Company, or if there are no such requirements or if the subject loan(s) are no longer outstanding, then within 45 days after the end of each of the first three quarters of each fiscal year, Company's quarterly, unaudited financial statements and within 90 days after the end of each fiscal year, Company's annual, audited financial statements.

(b) Exempt Transaction. The issuance of the Shares will each constitute a transaction exempt from (i) the registration requirements of Section 5 of the Act, in reliance upon Section 4(2) thereof and/or Regulation D thereunder, and (ii) the qualification requirements of applicable state securities laws.

(c) Compliance with Rule 144. If Holder proposes to sell the Shares issuable upon the exercise of this Warrant in compliance with Rule 144 promulgated by the SEC, then, upon Holder's written request to the Company, the Company shall furnish to Holder, within ten days after receipt of such request, a written statement confirming the Company's compliance with the filing requirements of the SEC as set forth in such rule (as may be amended from time to time).

3.5 Reserved.

ARTICLE 4 REPRESENTATIONS AND WARRANTIES OF HOLDER.

Holder represents and warrants to the Company as follows:

4.1 Purchase for Own Account. This Warrant and the Shares to be acquired upon exercise of this Warrant by Holder are being acquired for investment for Holder's account, not as a nominee or agent, and not with a view to the public resale or distribution within the meaning of the Act. Holder also represents that it has not been formed for the specific purpose of acquiring this Warrant or the Shares.

4.2 Disclosure of Information. Holder is aware of the Company's business affairs and financial condition and has received or has had full access to all the information it considers necessary or appropriate to make an informed investment decision with respect to the acquisition of this Warrant and its underlying securities. Holder further has had an opportunity to ask questions and receive answers from the Company regarding the terms and conditions of the offering of this Warrant and its underlying securities and to obtain additional information (to the extent the Company possessed such information or could acquire it without unreasonable effort or expense) necessary to verify any information furnished to Holder or to which Holder has access.

4.3 Investment Experience. Holder understands that the purchase of this Warrant and its underlying securities involves substantial risk. Holder has experience as an investor in securities of companies in the development stage and acknowledges that Holder can bear the economic risk of such Holder's investment in this Warrant and its underlying securities and has such knowledge and experience in financial or business matters that Holder is capable of evaluating the merits and risks of its investment in this Warrant and its underlying securities and/or has a preexisting personal or business relationship with the Company and certain of its officers, directors or

controlling persons of a nature and duration that enables Holder to be aware of the character, business acumen and financial circumstances of such persons.

4.4 Accredited Investor Status. Holder is an “accredited investor” within the meaning of Regulation D promulgated under the Act.

4.5 The Act. Holder understands that this Warrant and the Shares issuable upon exercise hereof have not been registered under the Act in reliance upon a specific exemption therefrom, which exemption depends upon, among other things, the bona fide nature of Holder’s investment intent as expressed herein. Holder understands that this Warrant and the Shares issued upon any exercise hereof must be held indefinitely unless subsequently registered under the Act and qualified under applicable state securities laws, or unless exemption from such registration and qualification are otherwise available. Holder is aware of the provisions of Rule 144 promulgated under the Act.

4.6 No Voting Rights. Holder, as a Holder of this Warrant, will not have any voting rights until the exercise of this Warrant.

ARTICLE 5 MISCELLANEOUS.

5.1 Legends. This Warrant and the Shares (and the securities issuable, directly or indirectly, upon conversion of Shares, if any) shall be imprinted with a legend in substantially the following form:

THIS SECURITY HAS NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, AND MAY NOT BE SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHOUT AN EFFECTIVE REGISTRATION THEREOF UNDER SUCH ACT OR PURSUANT TO RULE 144 OR AN OPINION OF COUNSEL REASONABLY SATISFACTORY TO COMPANY AND ITS COUNSEL THAT SUCH REGISTRATION IS NOT REQUIRED.

5.2 Compliance with Securities Laws on Transfer. This Warrant and the Shares issuable upon exercise of this Warrant (and the securities issuable, directly or indirectly, upon conversion of Shares, if any) may not be transferred or assigned in whole or in part without compliance with applicable federal and state securities laws by the transferor and the transferee (including, without limitation, the delivery of investment representation letters and legal opinions reasonably satisfactory to Company, as reasonably requested by Company). Company shall not require Holder to provide an opinion of counsel if the transfer is to Holder’s parent company, Western Alliance Bancorporation, or any other affiliate of Holder, or if there is no material question as to the availability of current information as referenced in Rule 144(c), Holder represents that it has complied with Rule 144(d) and (e) in reasonable detail, the selling broker represents that it has complied with Rule 144(f), and the Company is provided with a copy of Holder’s notice of proposed sale.

5.3 Transfer Procedure. After receipt by Holder of the executed Warrant, Holder may transfer all of this Warrant to Holder’s parent company, Western Alliance Bancorporation, or an affiliate thereof or successor thereto (the “Subsequent Holder”), by execution of an Assignment substantially in the form of Appendix 3. Subject to the provisions of Article 4.2 and upon providing Company with written notice, the Subsequent Holder may transfer all or part of this Warrant or the Shares issuable upon exercise of this Warrant (or the Shares issuable directly or indirectly, upon conversion of the Shares, if any) to any transferee, provided, however, in

connection with any such transfer, the Subsequent Holder will give the Company notice of the portion of the Warrant being transferred with the name, address and taxpayer identification number of the transferee and Holder will surrender this Warrant to the Company for reissuance to the transferee(s) (and Holder if applicable).

5.4 Notices. All notices and other communications from Company to Holder, or vice versa, shall be in writing and shall be deemed delivered and effective when given personally or mailed by first-class registered or certified mail, postage prepaid, or by overnight courier, at such address as may have been furnished to Company or Holder, as the case may be, in writing by Company or such Holder from time to time.

5.5 Attorneys Fees. In the event of any dispute between the parties concerning the terms and provisions of this Warrant, the party prevailing in such dispute shall be entitled to collect from the other party all costs incurred in such dispute, including reasonable attorneys' fees.

5.6 Governing Law. This Warrant shall be governed by and construed in accordance with the laws of the State of Arizona, without giving effect to its principles regarding conflicts of law.

[SIGNATURE PAGE FOLLOWS]

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

COMPANY:

BIOLASE, INC., a Delaware corporation

By: /s/ John R. Beaver

Name: John R. Beaver

Title: SVP & Chief Financial Officer

HOLDER:

WESTERN ALLIANCE BANK, an Arizona corporation

By: /s/ Victor Le

Name: Victor Le

Title: Vice President

APPENDIX 1

NOTICE OF EXERCISE

[Strike paragraph that does not apply.]

1. The undersigned hereby elects to purchase _____ shares of the Common Stock of Company pursuant to the terms of the attached Warrant, and tenders herewith payment of the purchase price of such shares in full.

1. The undersigned hereby elects to convert the attached Warrant into Shares/cash [strike one] in the manner specified in the Warrant. This conversion is exercised with respect to _____ of the Shares covered by the Warrant.

2. Please issue a certificate or certificates representing said shares in the name of the undersigned or in such other name as is specified below:

Name: _____

Address: _____

3. The undersigned represents it is acquiring the shares solely for its own account and not as a nominee for any other party and not with a view toward the resale or distribution thereof except in compliance with applicable securities laws.

WESTERN ALLIANCE BANK, an Arizona corporation

By:
Name:
Title:

APPENDIX 2

CAPITALIZATION TABLE

Not applicable

1693899.2

1

APPENDIX 3

ASSIGNMENT

For value received, WESTERN ALLIANCE BANK, hereby sells, assigns and transfers unto:

Name: WESTERN ALLIANCE BANCORPORATION
Address: One E. Washington, Suite 1400
Phoenix, Arizona 85004
Tax ID:

that certain Warrant to Purchase Stock issued by BIOLASE, INC., a Delaware corporation (the "Company"), on March 6, 2018 (the "Warrant") together with all rights, title and interest therein.

WESTERN ALLIANCE BANK

By:
Name:
Title:

By its execution below, and for the benefit of the Company, Western Alliance Bancorporation agrees to all other provisions of the Warrant as of the date hereof.

WESTERN ALLIANCE BANCORPORATION

By:
Name:
Title:

BUSINESS FINANCING AGREEMENT

Borrower: BIOLASE, INC.
BL ACQUISITION CORP.
BL ACQUISITION II INC.
4 Cromwell
Irvine, CA 92618

Lender: WESTERN ALLIANCE BANK, an Arizona corporation
55 Almaden Boulevard, Suite 100
San Jose, CA 95113

This BUSINESS FINANCING AGREEMENT, dated as of March 6, 2018 (the “**Closing Date**”), is made and entered into between WESTERN ALLIANCE BANK, an Arizona corporation (“**Lender**”) and BIOLASE, INC., a Delaware corporation (“**Parent**”), BL ACQUISITION CORP., a Delaware corporation (“**BL Acquisition**”), and BL ACQUISITION II INC., a Delaware corporation (“**BL Acquisition II**”, and together with Parent and BL Acquisition, individually and collectively, jointly and severally, “**Borrower**”), on the following terms and conditions:

1. REVOLVING CREDIT LINE.

- 1.1 Advances.** Subject to the terms and conditions of this Agreement, from the Closing Date until the Maturity Date, Lender agrees and will make Advances to Borrower from time to time not exceeding the Credit Limit (subject at all times to the Domestic Credit Limit and the EXIM Credit Limit) or the Borrowing Base (subject at all times to the Domestic Borrowing Base and EXIM Borrowing Base), whichever is less; provided that in no event shall Lender be obligated to make any Advance that results in an Overadvance or while any Overadvance is outstanding. Amounts borrowed under this Section may be repaid and subject to the terms and conditions hereof reborrowed during the term of this Agreement. It shall be a condition to each Advance that (a) an Advance Request acceptable to Lender has been received by Lender, (b) all of the representations and warranties set forth in Section 3 are true and correct on the date of such Advance as though made at and as of each such date, and (c) no Default has occurred and is continuing, or would result from such Advance.
- 1.2 Advance Requests.** Borrower may request that Lender make an Advance by delivering to Lender an Advance Request therefor and Lender shall be entitled to rely on such information provided by Borrower to Lender on or with the Advance Request. Lender may honor Advance Requests, instructions or repayments given by any Authorized Person.
- 1.3 Due Diligence.** Lender may audit Borrower’s Receivables and any and all applicable records pertaining to the Collateral, at Lender’s sole discretion and at Borrowers expense, provided that such audits must be done during normal business hours and upon no less than three (3) Business Days’ advance notice to Borrower (provided no notice is required if an Event of Default has occurred and is continuing). Borrower acknowledges that such an audit must be completed prior to the initial Advance and at least once every six months thereafter. Lender may at any time and from time to time contact Account Debtors and other Persons obligated or knowledgeable in respect of Receivables to confirm the Receivable Amount of such Receivables, to determine whether Receivables constitute Eligible Receivables, and for any other purpose specifically in connection with this Agreement. If any of the Collateral or Borrower’s books or records pertaining to the Collateral are in the possession of a third party, Borrower authorizes that third party to permit Lender or its agents to have access to perform inspections or audits thereof and to respond to Lender’s requests for information concerning such Collateral and records.

1.4 Collections.

(a) Lender shall have the exclusive right to receive all Collections on all Receivables. Borrower shall (i) immediately notify, transfer and deliver to Lender all Collections Borrower receives for deposit into the Collection Account, (ii) deliver to Lender a detailed cash receipts journal on Friday of each week until the Collection Account is operational, and (iii) upon the request of Lender in its sole discretion, immediately enter into a collection services agreement acceptable to Lender (the “**Lockbox Agreement**”) pursuant to which all Collections received in the Lockbox shall be deposited into the Collection Account. Until the Lockbox is required by Lender, Borrower shall utilize an electronic deposit capture device with Lender for any payments made by check. Borrower shall use the Lender’s address as the remit to and payment address for all of Borrower’s Collections from Account Debtors, and Borrower shall instruct all Account Debtors to make payments either directly to the Collection Account or instruct them to deliver such payments to Lender by wire transfer, ACH, or other means as Lender may direct for deposit to the Lockbox (if applicable) or Collection Account. It will be considered an immediate Event of Default if this does not occur or the Lockbox is not operational within 30 days of Lender’s request.

(b) Lender shall transfer all Collections deposited into the Collection Account to Borrower’s Account on a daily basis; provided that upon the occurrence and during the continuance of any Default, Lender may apply all Collections to the Obligations in such order and manner as Lender may determine. Lender has no duty to do any act other than to apply such amounts as required above. If an item of Collections is not honored or Lender does not receive good funds for any reason, any amount previously transferred to Borrower’s Account or applied to the Account Balance shall be reversed as of the date transferred or applied, as applicable, and, if applied to the Account Balance, the Finance Charge will accrue as if the Collections had not been so applied. Lender shall have, with respect to any goods related to the Receivables, all the rights and remedies of an unpaid seller under the UCC and other applicable law, including the rights of replevin, claim and delivery, reclamation and stoppage in transit.

1.5 Receivables Activity Report. Within 30 days after the end of each Month End, Lender shall send to Borrower a report covering the transactions for the prior billing period, including the amount of all Advances, Collections, Adjustments, Finance Charges, and other fees and charges. The accounting shall be deemed correct and conclusive unless Borrower makes written objection to Lender within 30 days after Borrower’s receipt of such Lender accounting.

1.6 Adjustments. In the event any Adjustment or dispute is asserted by any Account Debtor, Borrower shall promptly advise Lender and shall, subject to Lender’s reasonable approval, resolve such disputes and advise Lender of any Adjustments; provided that in no case will the aggregate Adjustments made with respect to any individual Receivable over \$5,000 or aggregate Receivables over \$50,000 exceed two percent (2%) of its original Receivable Amount unless Borrower has obtained the prior written consent of Lender. So long as any Obligations are outstanding, Lender shall have the right, at any time, to take possession of any rejected, returned, or recovered personal property. If such possession is not taken by Lender, Borrower is to resell it for Lender’s account at Borrower’s expense with the proceeds made payable to Lender. While Borrower retains possession of any returned goods, Borrower shall segregate said goods and mark them as property of Lender.

- 1.7 Recourse; Maturity.** Advances and the other Obligations shall be with full recourse against Borrower. On the Maturity Date or such earlier date as shall be herein provided, Borrower will pay all then outstanding Advances and other Obligations to Lender.
- 1.8 Letter of Credit Line.** Subject to the terms and conditions of this Agreement, Lender hereby agrees to issue or cause an Affiliate to issue letters of credit for the account of Borrower (each, a "**Letter of Credit**" and collectively, "**Letters of Credit**") from time to time; provided that (a) the Letter of Credit Obligations shall not at any time exceed the International Sublimit less the FX Amount, and (b) the Letter of Credit Obligations will be treated as Advances for purposes of determining availability under the Domestic Credit Limit and shall decrease, on a dollar-for-dollar basis, the amount available for other Advances. The form and substance of each Letter of Credit shall be subject to approval by Lender, in its sole discretion. Each Letter of Credit shall be subject to the additional terms of the Letter of Credit agreements, applications and any related documents required by Lender in connection with the issuance thereof (each, a "**Letter of Credit Agreement**"). Each draft paid under any Letter of Credit shall be repaid by Borrower in accordance with the provisions of the applicable Letter of Credit Agreement. No Letter of Credit shall be issued that results in an Overadvance or while any Overadvance is outstanding. Upon the Maturity Date, the amount of Letter of Credit Obligations shall be secured by unencumbered cash on terms acceptable to Lender if the term of this Agreement is not extended by Lender.
- 1.9 Cash Management Services.** Borrower may use availability hereunder up to the Cash Management Sublimit for Lender's cash management services, which may include merchant services, direct deposit of payroll, business credit card, and check cashing services identified in various cash management services agreements related to such services (the "**Cash Management Services**"). The amount of Obligations with respect to Cash Management Services, including, without limitation, the total availability under all business credit cards, will be treated as an Advance for purposes of determining availability under the Domestic Credit Limit and shall decrease, on a dollar-for-dollar basis, the amount available for other Advances. The Cash Management Services shall be subject to additional terms set forth in applicable cash management services agreements. Upon the Maturity Date, the amount of Obligations with respect to Cash Management Services shall be secured by unencumbered cash on terms acceptable to Lender if the term of this Agreement is not extended by Lender.
- 1.10 Foreign Exchange Facility.** Subject to and upon the terms and conditions of this Agreement and any other agreement that Borrower may enter into with Lender in connection with foreign exchange transactions ("**FX Contracts**") and subject to the availability under the Domestic Credit Limit and the Domestic Borrowing Base, Borrower may request Lender to enter into FX Contracts with Borrower, which shall be due no later than the Maturity Date unless cash secured on terms satisfactory to Lender. Borrower shall conduct all its United States foreign currency exchange business through Lender. Borrower shall pay any standard issuance and other fees that Lender notifies Borrower will be charged for issuing and processing FX Contracts for Borrower. The FX Amount (a) shall at all times be equal to or less than the International Sublimit less any amounts outstanding under the Letter of Credit Sublimit and (b) will be treated as an Advance for purposes of determining availability under the Domestic Credit Limit and shall decrease, on a dollar-for-dollar basis, the amount available for other Advances. The "FX Amount" shall equal the amount determined by multiplying (i) the aggregate amount, in United States Dollars, of FX Contracts between Borrower and Lender outstanding as of any date of determination by (ii) the applicable Foreign Exchange Reserve Percentage as of such date. The "Foreign Exchange Reserve Percentage" shall be a percentage as determined by Lender, in its sole discretion from time to time.

- 1.11 Overadvances.** Upon any occurrence of an Overadvance, Borrower shall immediately pay down the Advances such that, after giving effect to such payments, no Overadvance exists.
- 1.12 Notification and Verification.** Lender may (i) verify outstanding invoices and (ii) notify Borrower's Account Debtors of Lender's security interest in the Receivables, at its sole discretion from time to time.

2. FEES AND FINANCE CHARGES.

2.1 Finance Charges. Borrower agrees to pay to Lender the Finance Charges on the Account Balance. Lender may, but is not required to, deduct the amount of accrued Finance Charges from Collections received by Lender. The accrued and unpaid Finance Charges shall be due and payable within 10 calendar days after each Month End during the term hereof.

2.2 Fees.

- (a) **Domestic Facility Fee.** Borrower shall pay the Domestic Facility Fee to Lender promptly upon the execution of this Agreement and annually thereafter.
- (b) **EXIM Facility Fee.** Borrower shall pay the EXIM Facility Fee to Lender promptly upon the execution of this Agreement and annually thereafter.
- (c) **EXIM Application Fee.** Borrower shall pay the EXIM Application Fee to Lender promptly upon the execution of this Agreement.
- (d) **Letter of Credit Fees.** Borrower shall pay to Lender fees upon the issuance of each Letter of Credit, upon the payment or negotiation of each draft under any Letter of Credit and upon the occurrence of any other activity with respect to any Letter of Credit (including without limitation, the transfer, amendment or cancellation of any Letter of Credit) determined in accordance with Lender's standard fees and charges then in effect for such activity.
- (e) **Cash Management and FX Contract Fees.** Borrower shall pay to Lender fees in connection with the Cash Management Services and the FX Contracts as determined in accordance with Lender's standard fees and charges then in effect for such activity.
- (f) **Due Diligence Fee.** Borrower shall pay the Due Diligence Fee to Lender promptly upon the execution of this Agreement and annually thereafter.
- (g) **Due Diligence Deposit.** Borrower has paid to Lender a due diligence deposit of \$15,000, which deposit shall be applied to the Domestic Facility Fee and Lender's expenses on the Closing Date.

3. REPRESENTATIONS AND WARRANTIES. Borrower represents and warrants:

3.1 No representation, warranty or other statement of Borrower in any certificate or written statement given to Lender contains any untrue statement of a material fact or omits to state a material fact necessary to make the statement contained in the certificates or statement not misleading.

- 3.2** Borrower is duly existing and in good standing in its jurisdiction of formation and qualified and licensed to do business in, and in good standing in, any jurisdiction in which the conduct of its business or its ownership of property requires that it be qualified, except where the failure to do so could not reasonably be expected to have a material adverse effect on Borrower's business.
- 3.3** The execution, delivery and performance of this Agreement has been duly authorized, does not (a) conflict with Borrower's organizational documents, (b) contravene, conflict with, constitute a default under or violate any material Requirement of Law, (c) contravene, conflict or violate any applicable order, writ, judgment, injunction, decree, determination or award of any Governmental Authority by which Borrower or any of Borrower's property or assets may be bound or affected, (d) require any action by, filing, registration, or qualification with, or Governmental Approval from, any Governmental Authority (except such Governmental Approvals which have already been obtained and are in full force and effect), or (e) constitute an Event of Default under any material agreement by which Borrower is bound. Borrower is not in default under any agreement to which or by which it is bound.
- 3.4** Borrower has not violated any laws, ordinances or rules, the violation of which could have a material adverse effect on Borrower's business.
- 3.5** Borrower has good title to the Collateral and all inventory is in all material respects of good and marketable quality, free from material defects.
- 3.6** Borrower's name, form of organization, chief executive office, and the place where the records concerning all Receivables and Collateral are kept is set forth at the beginning of this Agreement, Borrower is located at its address for notices set forth in this Agreement.
- 3.7** If Borrower owns, holds or has any interest in, any copyrights (whether registered, or unregistered), patents or trademarks, and licenses of any of the foregoing, such interest has been specifically disclosed and identified to Lender in writing.
- 3.8** Borrower is the sole owner of the intellectual property which it owns or purports to own, except for non-exclusive licenses granted by Borrower to its customers in the ordinary course of business. Each of the patents is valid and enforceable, and no part of the intellectual property has been judged invalid or unenforceable, in whole or in part, and no claim has been made that any part of the intellectual property violates the rights of any third party.
- 3.9** Borrower is solvent and able to pay its debts (including trade debts) as they mature.
- 3.10** The Collateral is not in the possession of any third party bailee (such as a warehouse) except as otherwise disclosed in writing to Lender. None of the Collateral is currently being maintained at locations other than as disclosed in writing to Lender.
- 3.11** Except as disclosed in writing to Lender, there are no actions or proceedings pending or, to the knowledge of Borrower's officers, threatened in writing by or against Borrower or any Subsidiary in which an adverse decision could reasonably be expected to cause a Material Adverse Change.
- 3.12** All consolidated financial statements for Borrower and any Subsidiary delivered to Lender fairly present in all material respects Borrower's consolidated financial condition and Borrower's consolidated results of operations as of the date thereof and for the periods set forth therein. All consolidating financial statements for Borrower and its Subsidiaries delivered to Lender fairly

present in all material respects Borrower's and each of its Subsidiary's financial condition and results of operations as of the date thereof and for the periods set forth therein. There has not been any material deterioration in Borrower's consolidated financial condition since the date of the most recent financial statements submitted to Lender.

- 3.13 Borrower does not own any stock, partnership interest, other ownership interest or other equity securities except for Permitted Investments.
- 3.14 Borrower and each Subsidiary have timely filed all required tax returns and reports, and Borrower and each Subsidiary have timely paid all foreign, federal, state and local taxes, assessments, deposits and contributions owed by Borrower and each Subsidiary.

4. MISCELLANEOUS PROVISIONS. Borrower will:

- 4.1 Maintain its corporate existence and good standing in its jurisdiction of incorporation and maintain its qualification in each jurisdiction necessary to Borrower's business or operations and not merge or consolidate with or into any other business organization, or acquire all or substantially all of the capital stock or property of a third party, unless (i) any such acquired entity becomes a "borrower" under this Agreement and (ii) Lender has previously consented to the applicable transaction in writing.
- 4.2 Comply with all laws, ordinances and regulations to which it is subject, noncompliance with which could have a material adverse effect on Borrower's business.
- 4.3 Give Lender at least 30 days prior written notice of changes to its name, organization, chief executive office, location of records or otherwise add any new business locations or any new locations where Borrower intends to store Collateral, and, if requested by Lender, Borrower will cause the applicable landlord/bailee to enter into a landlord consent (or bailee agreement in the case of any bailee) in favor of Lender prior to the commencement of such new office or location.
- 4.4 Pay all its taxes including gross payroll, withholding and sales taxes when due and will deliver satisfactory evidence of payment to Lender if requested.
- 4.5 Maintain:
 - (a) insurance satisfactory to Lender as to amount, nature and carrier covering property damage (including loss of use and occupancy) to any of Borrower's properties, business interruption insurance, public liability insurance including coverage for contractual liability, product liability and workers' compensation, and any other insurance which is usual for Borrower's business. Each such policy shall provide for at least thirty (30) days prior notice to Lender of any cancellation thereof.
 - (b) all risk property damage insurance policies (including without limitation windstorm coverage, and hurricane coverage as applicable) covering the tangible property comprising the collateral. Each insurance policy must be for the full replacement cost of the collateral and include a replacement cost endorsement, or in an amount acceptable to Lender. The insurance must be issued by an insurance company acceptable to Lender and must include a lender's loss payable endorsement in favor of Lender in a form acceptable to Lender and Lender shall be named as an additional insured with respect to public liability insurance including coverage for contractual liability, product liability and workers' compensation.

Upon the request of Lender, Borrower shall deliver to Lender a copy of each insurance policy, or, if permitted by Lender, a certificate of insurance listing all insurance in force.

- 4.6 Immediately transfer and deliver to Lender all Collections Borrower receives.
- 4.7 Not create, incur, assume, or be liable for any indebtedness, other than Permitted Indebtedness.
- 4.8 Not convey, sell, lease, transfer or otherwise dispose of (collectively, a “**Transfer**”), all or any part of its business or property, other than: (a) Transfers of inventory in the ordinary course of business; (b) Transfers of non-exclusive licenses and similar arrangements for the use of the property of Borrower in the ordinary course of business; or (c) Transfers of worn-out or obsolete equipment which was not financed by Lender.
- 4.9 Not make any investment in or to any Person, other than Permitted Investments.
- 4.10 Not pay any dividends or make any distributions or payment with respect to Borrower’s capital stock or redeem, retire or purchase any of Borrower’s capital stock.
- 4.11 Not directly or indirectly enter into or permit to exist any material transaction with any Affiliate of Borrower except for transactions that are in the ordinary course of Borrower’s business, upon fair and reasonable terms that are no less favorable to Borrower than would be obtained in an arm’s length transaction with a non-affiliated Person.
- 4.12 Not make any payment in respect of any Subordinated Debt or permit any of its Subsidiaries to make any such payment, except in compliance with the terms of the applicable subordination agreement in favor of Lender, or amend any provision contained in any documentation relating to the Subordinated Debt without Lender’s prior written consent.
- 4.13 Immediately notify Lender if Borrower hereafter obtains any interest in any copyrights, patents, trademarks or licenses that are materially significant in value or are material to the conduct of its business.
- 4.14 Provide the following financial information and statements in form and content acceptable to Lender, and such additional information as reasonably requested by Lender in writing from time to time. Lender has the right to require Borrower to deliver financial information and statements to Lender more frequently than otherwise provided below, and to use such additional information and statements to measure any applicable financial covenants in this Agreement.
 - (a) No later than 30 days after the end of each month (including the last period in each fiscal year), monthly financial statements of Borrower, certified and dated by an authorized financial officer. The statements shall be prepared on a consolidated basis and, prior to the Subsidiary Dissolution (as defined below), on a consolidating basis.
 - (b) Promptly, upon sending or receipt, copies of any management letters and correspondence relating to management letters, sent or received by Borrower to or from Borrower's auditor. If no management letter is prepared, Borrower shall, upon Lender's request, obtain a letter from such auditor stating that no deficiencies were noted that would otherwise be addressed in a management letter.

- (c) Copies of the Form 10-K Annual Report, Form 10-Q Quarterly Report and Form 8-K Current Report for Borrower within 5 days of the date of filing with the Securities and Exchange Commission.
 - (d) Annual board-approved financial projections and operating budgets specifying the assumptions used in creating the projections and budgets. Annual board-approved projections and budgets shall in any case be provided to Lender no later than 30 days after the beginning of each fiscal year.
 - (e) Within 5 days of filing, copies of all business tax returns, which must be prepared by a Certified Public Accountant acceptable to Lender.
 - (f) Within 30 days of the end of each month, a Compliance Certificate of Borrower, signed by an authorized financial officer and setting forth (i) the information and computations (in sufficient detail) to establish compliance with all financial covenants at the end of the period covered by the financial statements then being furnished and (ii) whether there existed as of the date of such financial statements and whether there exists as of the date of the certificate, any default under this Agreement and, if any such default exists, specifying the nature thereof and the action Borrower is taking and proposes to take with respect thereto.
 - (g) Within 15 days after the end of each calendar month, (i) a domestic borrowing base certificate, in form and substance satisfactory to Lender, setting forth Domestic Eligible Receivables and Receivable Amounts thereof as of the last day of the preceding reporting period, and (ii) an EXIM borrowing base certificate, in form and substance satisfactory to Lender, setting forth EXIM Eligible Receivables and Receivable Amounts thereof as of the last day of the preceding reporting period.
 - (h) Within 15 days after the end of each calendar month, detailed agings of Borrower's accounts receivable and accounts payable by invoice date and detailed agings of Borrower's accounts receivable and accounts payable by due date, in each case, separating domestic receivables and EXIM receivables, together with a deferred revenue report and such other matters as Lender may request.
 - (i) Within 30 days after the end of each calendar quarter, a quarterly invoice sampling certified by an authorized financial officer and in form and substance satisfactory to Lender.
 - (j) Promptly upon Lender's request, such other books, records, statements, lists of property and accounts, budgets, forecasts or reports as to Borrower and as to each guarantor of Borrower's obligations to Lender as Lender may reasonably request.
- 4.15** Within 90 days of the Closing Date and at all times thereafter, maintain all of its and its Subsidiaries' depository and operating accounts and investment accounts with Lender, and, in the case of any accounts not maintained with Lender, grant to Lender a first priority perfected security interest in and "control" (within the meaning of Section 47-9104 of the Arizona Uniform Commercial Code) of such account pursuant to documentation acceptable to Lender.

- 4.16** Provide to Lender promptly upon the execution hereof, and as a condition to the effectiveness of this Agreement, the following documents which shall be in form satisfactory to Lender: (i) EXIM Documents; (ii) an intellectual property security agreement, duly executed by Borrower, (iii) Corporate Resolutions to Borrow, duly executed by Borrower, and (iv) a warrant to purchase stock, duly executed by Borrower.
- 4.17** Within 30 days of the Closing Date, and as a condition precedent to the initial Advance hereunder, provide to Lender the following documents which shall be in form satisfactory to Lender: (i) a deposit account control agreement, duly executed by Borrower and Comerica Bank, and (ii) a landlord waiver, duly executed by the landlord of Borrower's leased premises.
- 4.18** Within 90 days of the Closing Date, provide to Lender evidence satisfactory to Lender that Borrower has dissolved the following entities (the "**Subsidiary Dissolution**"): Biolase International, LLC, a Delaware limited liability company, Societe EndoTechnic, Inc., a California corporation, and Occulase, Inc., a Delaware corporation.
- 4.19** Promptly provide to Lender such additional information and documents regarding the finances, properties, business or books and records of Borrower or any guarantor or any other obligor as Lender may reasonably request.
- 4.20** At all times that Advances are outstanding hereunder, maintain Borrower's financial condition as follows in accordance with GAAP and used consistently with prior practices (except to the extent modified by the definitions herein):
- (a) Adjusted Quick Ratio, tested as of the end of each month, not at any time less than 1.00 to 1.00.
- (b) Revenues, measured on a trailing six (6) month basis as of the last day of each quarter set forth below, of not less than the following amounts for the following periods:

Trailing 6 Months Ending	Minimum Trailing 6-Month Revenue
March 31, 2018	\$20,028,000
June 30, 2018	\$21,360,000
September 30, 2018	\$22,800,000
December 31, 2018	\$24,560,000
March 31, 2018 and thereafter	Minimum revenue requirements for 2019 shall be determined by Lender, in consultation with Borrower, upon Lender's receipt of Borrower's 2019 board-approved financial projections due in accordance with Section 4.14(d) above, which should have, at a minimum, a similar growth rate from 2017 to 2018.

Notwithstanding the foregoing, if no Advances are outstanding and Borrower requests an Advance, it shall be a condition to such Advance that Borrower deliver to Lender, in addition to any other requirements set forth herein, evidence satisfactory to Lender that Borrower was in compliance with the covenants set forth in this Section 4.20 as of the most recently ended measuring period applicable to such covenant.

- 4.21** Not make or contract to make, without Lender's prior written consent, capital expenditures, including leasehold improvements, in any fiscal year in excess of \$150,000 or incur liability for rentals of property (including both real and personal property) in an amount which, together with capital expenditures, shall in any fiscal year exceed such sum.
- 4.22** Execute any further instruments and take further action as Lender requests to perfect or continue Lender's security interest in the Collateral or to effect the purposes of this Agreement.

5. SECURITY INTEREST. To secure the prompt payment and performance to Lender of all of the Obligations, Borrower hereby grants to Lender a continuing security interest in the Collateral. Borrower is not authorized to sell, assign, transfer or otherwise convey any Collateral without Lender's prior written consent, except for the sale of finished inventory in Borrower's usual course of business. Borrower agrees to sign any instruments and documents requested by Lender to evidence, perfect, or protect the interests of Lender in the Collateral. Borrower agrees to deliver to Lender the originals of all instruments, chattel paper and documents evidencing or related to Receivables and Collateral. Borrower shall not grant or permit any lien or security in the Collateral or any interest therein other than Permitted Liens.

6. POWER OF ATTORNEY . Borrower irrevocably appoints Lender and its successors and as true and lawful attorney in fact, and authorizes Lender (a) to, whether or not there has been an Event of Default, (i) demand, collect, receive, sue, and give releases to any Account Debtor for the monies due or which may become due upon or with respect to the Receivables and to compromise, prosecute, or defend any action, claim, case or proceeding relating to the Receivables, including the filing of a claim or the voting of such claims in any bankruptcy case, all in Lender's name or Borrower's name, as Lender may choose; (ii) prepare, file and sign Borrower's name on any notice, claim, assignment, demand, draft, or notice of or satisfaction of lien or mechanics' lien or similar document; (iii) notify all Account Debtors with respect to the Receivables to pay Lender directly; (iv) receive and open all mail addressed to Borrower for the purpose of collecting the Receivables; (v) endorse Borrower's name on any checks or other forms of payment on the Receivables; (vi) execute on behalf of Borrower any and all instruments, documents, financing statements and the like to perfect Lender's interests in the Receivables and Collateral; (vii) debit any Borrower's deposit accounts maintained with Lender for any and all Obligations due under this Agreement; and (viii) do all acts and things necessary or expedient, in furtherance of any such purposes, and (b) to, upon the occurrence and during the continuance of an Event of Default, sell, assign, transfer, pledge, compromise, or discharge the whole or any part of the Receivables. Upon the occurrence and continuation of an Event of Default, all of the power of attorney rights granted by Borrower to Lender hereunder shall be applicable with respect to all Receivables and all Collateral.

7. DEFAULT AND REMEDIES.

7.1 **Events of Default.** The occurrence of any one or more of the following shall constitute an Event of Default hereunder.

- (a) **Failure to Pay.** Borrower fails to make a payment when due under this Agreement.
- (b) **Lien Priority.** Lender fails to have an enforceable first lien (except for any prior liens to which Lender has consented in writing) on or security interest in the Collateral.
- (c) **False Information.** Borrower (or any guarantor) has given Lender any materially false or misleading information or representations or has failed to disclose any material fact relating to the subject matter of this Agreement.
- (d) **Death.** Any guarantor dies or becomes legally incompetent, or if such guarantor is a partnership, any general partner dies or becomes legally incompetent.
- (e) **Bankruptcy.** Borrower (or any guarantor) files a bankruptcy petition, a bankruptcy petition is filed against Borrower (or any guarantor) or Borrower (or any guarantor) makes a general assignment for the benefit of creditors.
- (f) **Receivers.** A receiver or similar official is appointed for a substantial portion of Borrower's (or any guarantor's) business, or the business is terminated.
- (g) **Judgments.** Any judgments or arbitration awards are entered against Borrower (or any guarantor), or Borrower (or any guarantor) enters into any settlement agreements with respect to any litigation or arbitration and the aggregate amount of all such judgments, awards, and agreements exceeds \$100,000.
- (h) **Material Adverse Change.** A Material Adverse Change occurs or is reasonably likely to occur.
- (i) **Cross-default.** Any default occurs under any agreement in connection with any credit Borrower (or any guarantor) or any of Borrower's Affiliates has obtained from anyone else or which Borrower (or any guarantor) or any of Borrower's Affiliates has guaranteed (other than trade amounts payable incurred in the ordinary course of business and not more than 60 days past due).
- (j) **Default under Related Documents.** Any default occurs under any guaranty, subordination agreement, security agreement, deed of trust, mortgage, or other document required by or delivered in connection with this Agreement or any such document is no longer in effect.
- (k) **Other Agreements.** Borrower (or any guarantor) or any of Borrower's Affiliates fails to meet the conditions of, or fails to perform any obligation under, any other agreement Borrower (or any guarantor) or any of Borrower's Affiliates has with Lender or any Affiliate of Lender.
- (l) **Change in Control.** A Change in Control occurs.
- (m) **Other Breach Under Agreement.** Borrower fails to meet the conditions of, or fails to perform any obligation under, any term of this Agreement not specifically referred to above.

7.2 Remedies. Upon the occurrence and during the continuance of an Event of Default, (1) without implying any obligation to do so, Lender may cease making Advances or extending any other financial accommodations to Borrower; (2) all or a portion of the Obligations shall be, at the option of and upon demand by Lender, or with respect to an Event of Default described in Section 7.1(e), automatically and without notice or demand, due and payable in full; and (3) Lender shall have and may exercise all the rights and remedies under this Agreement and under applicable law, including the rights and remedies of a secured party under the UCC, all the power of attorney rights described in Section 6 with respect to all Collateral, and the right to collect, dispose of, sell, lease, use, and realize upon all Receivables and all Collateral in any commercially reasonable manner.

8. ACCRUAL OF INTEREST. All interest and finance charges hereunder calculated at an annual rate shall be based on a year of 360 days, which results in a higher effective rate of interest than if a year of 365 or 366 days were used. Lender may charge interest, finance charges and fees based upon the projected amounts thereof as of the due dates therefor and adjust subsequent charges to account for the actual accrued amounts. If any amount due under Section 2.2, amounts due under Section 9, and any other Obligations not otherwise bearing interest hereunder is not paid when due, such amount shall bear interest at a per annum rate equal to the Finance Charge Percentage until the earlier of (i) payment in good funds or (ii) entry of a trial judgment thereof, at which time the principal amount of any money judgment remaining unsatisfied shall accrue interest at the highest rate allowed by applicable law.

9. FEES, COSTS AND EXPENSES; INDEMNIFICATION. Borrower will pay to Lender upon demand all fees, costs and expenses (including EXIM Bank Expenses, fees of attorneys and professionals and their costs and expenses) that Lender incurs or may from time to time impose in connection with any of the following: (a) preparing, negotiating, administering, and enforcing this Agreement or any other agreement executed in connection herewith, including any amendments, waivers or consents in connection with any of the foregoing, (b) any litigation or dispute (whether instituted by Lender, Borrower or any other Person) in any way relating to the Receivables, the Collateral, this Agreement or any other agreement executed in connection herewith or therewith, (c) enforcing any rights against Borrower or any guarantor, or any Account Debtor, (d) protecting or enforcing its interest in the Receivables or the Collateral, (e) collecting the Receivables and the Obligations, or (f) the representation of Lender in connection with any bankruptcy case or insolvency proceeding involving Borrower, any Receivable, the Collateral, any Account Debtor, or any guarantor. Borrower shall indemnify and hold Lender harmless from and against any and all claims, actions, damages, costs, expenses, and liabilities of any nature whatsoever arising in connection with any of the foregoing.

10. INTEGRATION, SEVERABILITY WAIVER, CHOICE OF LAW, FORUM AND VENUE.

10.1 This Agreement and any related security or other agreements required by this Agreement, collectively: (a) represent the sum of the understandings and agreements between Lender and Borrower concerning this credit; (b) replace any prior oral or written agreements between Lender and Borrower concerning this credit; and (c) are intended by Lender and Borrower as the final, complete and exclusive statement of the terms agreed to by them. In the event of any conflict between this Agreement and any other agreements required by this Agreement, this Agreement will prevail. If any provision of this Agreement is deemed invalid by reason of law, this Agreement will be construed as not containing such provision and the remainder of the Agreement shall remain in full force and effect. Lender retains all of its rights, even if it makes an Advance after a default. If Lender waives a default, it may enforce a later default. Any consent or waiver under, or amendment of, this Agreement must be in writing, and no such consent, waiver, or amendment shall imply any obligation by Lender to make any subsequent consent, waiver, or amendment.

10.2 THIS AGREEMENT SHALL BE GOVERNED BY AND INTERPRETED IN ACCORDANCE WITH THE INTERNAL LAWS OF THE STATE OF ARIZONA. THE PARTIES HERETO AGREE THAT ALL ACTIONS OR PROCEEDINGS ARISING IN CONNECTION WITH THIS AGREEMENT OR ANY OTHER RELATED DOCUMENTS SHALL BE TRIED AND LITIGATED ONLY IN THE STATE AND FEDERAL COURTS LOCATED IN THE COUNTY OF MARICOPA, ARIZONA, OR, AT THE SOLE OPTION OF LENDER, IN ANY OTHER COURT IN WHICH LENDER SHALL INITIATE LEGAL OR EQUITABLE PROCEEDINGS AND WHICH HAS JURISDICTION OVER THE SUBJECT MATTER AND PARTIES IN CONTROVERSY. EACH PARTY HERETO WAIVES ANY RIGHT TO ASSERT THE DOCTRINE OF FORUM NON CONVENIENS OR TO OBJECT TO VENUE TO THE EXTENT ANY PROCEEDING IS BROUGHT IN ACCORDANCE WITH THIS SECTION AND STIPULATES THAT THE STATE AND FEDERAL COURTS LOCATED IN THE COUNTY OF MARICOPA, ARIZONA SHALL HAVE IN PERSONAM JURISDICTION AND VENUE OVER EACH SUCH PARTY FOR THE PURPOSE OF LITIGATING ANY SUCH DISPUTE, CONTROVERSY, OR PROCEEDING ARISING OUT OF OR RELATED TO THIS AGREEMENT, OR ANY OTHER RELATED DOCUMENTS. SERVICE OF PROCESS SUFFICIENT FOR PERSONAL JURISDICTION IN ANY ACTION AGAINST BORROWER MAY BE MADE BY REGISTERED OR CERTIFIED MAIL, RETURN RECEIPT REQUESTED, TO ITS ADDRESS SPECIFIED FOR NOTICES PURSUANT TO SECTION 11.

11. NOTICES; TELEPHONIC AND TELEFAX AUTHORIZATIONS. All notices shall be given to Lender and Borrower at the addresses or faxes set forth on the signature page of this agreement and shall be deemed to have been delivered and received: (a) if mailed, three (3) calendar days after deposited in the United States mail, first class, postage pre-paid, (b) one (1) calendar day after deposit with an overnight mail or messenger service; or (c) on the same date of confirmed transmission if sent by hand delivery, telecopy, telefax or telex. Lender may honor telephone or telefax instructions for Advances or repayments given, or purported to be given, by any one of the Authorized Persons. Borrower will indemnify and hold Lender harmless from all liability, loss, and costs in connection with any act resulting from telephone or telefax instructions Lender reasonably believes are made by any Authorized Person. This paragraph will survive this Agreement's termination, and will benefit Lender and its officers, employees, and agents.

12. DEFINITIONS AND CONSTRUCTION.

12.1 Definitions. In this Agreement:

“**Account Balance**” means at any time the aggregate of the Advances outstanding as reflected on the records maintained by Lender, together with any past due Finance Charges thereon.

“**Account Debtor**” has the meaning in the UCC and includes any Person liable on any Receivable, including without limitation, any guarantor of any Receivable and any issuer of a letter of credit or banker's acceptance assuring payment thereof.

“**Adjusted Quick Ratio**” means (i) the aggregate of unrestricted cash and Cash Equivalents maintained with Lender plus net trade accounts receivable divided by (ii) (a) total current liabilities (including all Obligations to Lender) minus (b) the current portion of Deferred Revenue.

“**Adjustments**” means all discounts, allowances, disputes, offsets, defenses, rights of recoupment, rights of return, warranty claims, or short payments, asserted by or on behalf of any Account Debtor with respect to any Receivable.

“**Advance**” means an advance made by Lender to Borrower under this Agreement.

“**Advance Rate**” means (i) up to seventy-five percent (75%) in the case of Domestic Eligible Receivables, or (ii) up to eighty-five percent (85%) in the case of EXIM Eligible Receivables, or in each case, such greater or lesser percentage as Lender may from time to time establish in its sole discretion upon notice to Borrower.

“**Advance Request**” means a writing in form and substance satisfactory to Lender and signed by an Authorized Person requesting an Advance.

“**Affiliate**” means, as to any Person, any other Person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such Person.

“**Agreement**” means this Business Financing Agreement.

“**Authorized Person**” means any one of the individuals authorized to sign on behalf of Borrower.

“**Biolase India**” means Biolase India Private Limited, a wholly-owned Subsidiary of Biolase International and Occulase.

“**Borrower Agreement**” is the Export-Import Bank of the United States Working Capital Guarantee Program Borrower Agreement executed by Borrower in favor of EXIM Bank and Lender.

“**Borrower’s Account**” means Borrower’s general operating account maintained with Lender, into which Advances will be deposited unless otherwise instructed by Borrower in writing.

“**Borrowing Base**” means at any time the sum of (i) the Domestic Borrowing Base plus (ii) the EXIM Borrowing Base.

“**Cash Equivalents**” means (i) marketable direct obligations issued or unconditionally guaranteed by the United States of America or any agency or any State thereof maturing within one (1) year from the date of acquisition thereof, (ii) commercial paper maturing no more than one (1) year from the date of creation thereof and currently having rating of at least A-2 or P-2 from either Standard & Poor’s Corporation or Moody’s Investors Service, and (iii) certificates of deposit maturing no more than one (1) year from the date of investment therein issued by Lender.

“**Cash Management Sublimit**” means \$500,000.

“Change in Control” shall mean (a) a transaction in which any “person” or “group” (within the meaning of Section 13(d) and 14(d)(2) of the Securities Exchange Act of 1934) becomes the “beneficial owner” (as defined in Rule 13d-3 under the Securities Exchange Act of 1934), directly or indirectly, of a sufficient number of shares of all classes of stock then outstanding of Parent ordinarily entitled to vote in the election of directors, empowering such “person” or “group” to elect a majority of the Board of Directors of Parent, who did not have such power before such transaction, (b) any Subsidiary of Parent (other than Biolase India) ceases to be wholly-owned by Parent or (c) Biolase India ceases to be owned solely by Biolase International and/or Occulase.

“Collateral” means all of Borrower’s rights and interest in any and all personal property, whether now existing or hereafter acquired or created and wherever located, and all products and proceeds thereof and accessions thereto, including but not limited to the following (collectively, the “Collateral”): (a) all accounts (including health care insurance receivables), chattel paper (including tangible and electronic chattel paper), inventory (including all goods held for sale or lease or to be furnished under a contract for service, and including returns and repossessions), equipment (including all accessions and additions thereto), instruments (including promissory notes), investment property (including securities and securities entitlements), documents (including negotiable documents), deposit accounts, letter of credit rights, money, any commercial tort claim of Borrower which is now or hereafter identified by Borrower or Lender, general intangibles (including payment intangibles, intellectual property and software), goods (including fixtures) and all of Borrower’s books and records with respect to any of the foregoing, and the computers and equipment containing said books and records; and (b) any and all cash proceeds and/or noncash proceeds thereof, including without limitation, insurance proceeds, and all supporting obligations and the security therefore or for any right to payment.

“Collection Account” means the deposit account maintained with Lender which, pursuant to the Lockbox Agreement, all Collections received in the Lockbox are to be deposited, and as to which Borrower has no right to withdraw funds.

“Collections” means all payments from or on behalf of an Account Debtor with respect to Receivables.

“Compliance Certificate” means a certificate in the form attached as Exhibit A to this Agreement by an Authorized Person that, among other things, the representations and warranties set forth in this Agreement are true and correct as of the date such certificate is delivered.

“Credit Limit” means \$6,000,000, which is intended to be the maximum amount of Advances at any time outstanding.

“Default” means any Event of Default or any event that with notice, lapse of time or otherwise would constitute an Event of Default.

“Deferred Revenue” is all amounts received or invoiced, as appropriate, in advance of performance under contracts and not yet recognized as revenue.

“Domestic Borrowing Base” means at any time the difference of (i) the Domestic Eligible Receivable Amount multiplied by the applicable Advance Rate, minus (ii) such reserves as Lender may deem proper and necessary from time to time.

“Domestic Credit Limit” means \$6,000,000, which is intended to be the maximum amount of Advances at any time outstanding with respect to Domestic Eligible Receivables.

“Domestic Eligible Receivable” means a Receivable that satisfies all of the following:

- (a) The Receivable has been created by Borrower in the ordinary course of Borrower’s business and without any obligation on the part of Borrower to render any further performance.
- (b) There are no conditions which must be satisfied before Borrower is entitled to receive payment of the Receivable, and the Receivable does not arise from COD sales, consignments, bill and hold, or guaranteed sales.
- (c) The Account Debtor upon the Receivable does not claim any defense to payment of the Receivable, whether well founded or otherwise.
- (d) The Receivable is not the obligation of an Account Debtor who has asserted or may reasonably be expected to assert any counterclaims or offsets against Borrower (including offsets for any “contra accounts” owed by Borrower to the Account Debtor for goods purchased by Borrower or for services performed for Borrower).
- (e) The Receivable represents a genuine obligation of the Account Debtor and to the extent any credit balances exist in favor of the Account Debtor, such credit balances shall be deducted in calculating the Receivable Amount.
- (f) Borrower has sent an invoice to the Account Debtor in the amount of the Receivable.
- (g) Borrower is not prohibited by the laws of the jurisdiction where the Account Debtor is located from bringing an action in the courts of that jurisdiction to enforce the Account Debtor’s obligation to pay the Receivable. Borrower has taken all appropriate actions to ensure access to the courts of the jurisdiction where Account Debtor is located, including, where necessary; the filing of a Notice of Business Activities Report or other similar filing with the applicable government agency or the qualification by Borrower as a foreign corporation authorized to transact business in such jurisdiction.
- (h) The Receivable is owned by Borrower free of any title defects or any liens or interests of others except the security interest in favor of Lender, and Lender has a perfected, first priority security interest in such Receivable.
- (i) The Account Debtor on the Receivable is not any of the following: (1) an employee, Affiliate, parent or Subsidiary of Borrower, or any Person which has common officers or directors with Borrower; (2) the U.S. government or any agency or department of the U.S. government unless Borrower complies with the procedures in the Federal Assignment of Claims Act of 1940 (41 U.S.C. §15) with respect to the Receivable, and the underlying contract expressly provides that neither the U.S. government nor any agency or department thereof shall have the right of set-off against Borrower; (3) any Person located in a foreign country; or (4) an Account Debtor as to which thirty-five percent (35%) or more of the aggregate dollar amount of all outstanding Receivables owing from such Account Debtor have not been paid within 90 days from invoice date.

- (j) The Receivable is not in default (a Receivable will be considered in default if any of the following occur: (i) the Receivable is not paid within 90 days from its invoice date; (ii) the Receivable has a credit balance over 90 days from its invoice date; (iii) the Account Debtor obligated upon the Receivable suspends business, makes a general assignment for the benefit of creditors, or fails to pay its debts generally as they come due; or (iv) any petition is filed by or against the Account Debtor obligated upon the Receivable under any bankruptcy law or any other law or laws for the relief of debtors).
- (k) The Receivable does not arise from the sale of goods which remain in Borrower's possession or under Borrower's control.
- (l) The Receivable is not a bonded Receivable and does not constitute a prebilling, prepaid deposit, retention billing or progress billing.
- (m) The Receivable is not owing from an Account Debtor with respect to which Borrower has received Deferred Revenue (but such Receivable shall only be offset to the extent of such Deferred Revenue), unless otherwise approved in writing by Lender in its sole discretion on a case-by-case basis.
- (n) The Receivable is not evidenced by a promissory note or chattel paper, nor is the Account Debtor obligated to Borrower under any other obligation which is evidenced by a promissory note.
- (o) The Receivable is not that portion of Receivables due from an Account Debtor which is in excess of thirty percent (30%) (forty percent (40%) for Dental One Partners, Highland Capital and Henry Schein) of Borrower's aggregate dollar amount of all outstanding Receivables.
- (p) The Receivable is otherwise acceptable to Lender.

"Domestic Eligible Receivable Amount" means at any time the sum of the Receivable Amounts of the Domestic Eligible Receivables.

"Domestic Facility Fee" means a fee equal to one-quarter of one percent (0.25%) of the Domestic Credit Limit due upon the Closing Date and each anniversary thereof so long as any Advances are outstanding or available hereunder.

"Domestic Line of Credit" means the revolving line of credit under which Borrower may request Lender to issue Advances with respect to Domestic Eligible Receivables up to the Domestic Credit Limit, as specified in Section 1.1 hereof.

"Domestic Overadvance" means at any time an amount equal to the greater of (a) the amount (if any) by which the total amount of the outstanding Advances with respect to Domestic Eligible Receivables (including deemed Advances with respect to the International Sublimit and the total amount of the Cash Management Sublimit) exceeds the lesser of the Domestic Credit Limit or the Domestic Borrowing Base, (b) the amount (if any) by which the total amount of the outstanding Advances (including deemed Advances with respect to the International Sublimit and the total amount of the Cash Management Sublimit) exceeds the Credit Limit, (c) the amount (if any) by which the total amount of the outstanding deemed Advances with respect to the International Sublimit exceed the International Sublimit, or (d) the amount (if any) by which the total amount of the outstanding deemed Advances with respect to the Cash Management Sublimit exceed the Cash Management Sublimit.

“**Due Diligence Fee**” means a payment of an annual fee equal to \$900 due upon the Closing Date and \$900 due upon each anniversary thereof so long as any Advance is outstanding or available hereunder.

“**Eligible Receivable**” means a Domestic Eligible Receivable or an EXIM Eligible Receivable.

“**EXIM Application Fee**” means a fee in the amount of \$100 due on the Closing Date.

“**EXIM Bank**” means Export-Import Bank of the United States.

“**EXIM Bank Expenses**” are all reasonable fees that Lender pays to the EXIM Bank in consideration of the issuance of the EXIM Guarantee.

“**EXIM Borrowing Base**” means at any time the difference of (i) the EXIM Eligible Receivable Amount multiplied by the applicable Advance Rate, minus (ii) such reserves as Lender may deem proper and necessary from time to time.

“**EXIM Credit Limit**” means \$3,000,000, which is intended to be the maximum amount of Advances at any time outstanding with respect to EXIM Eligible Receivables.

“**EXIM Documents**” means the EXIM Guarantee, the Borrower Agreement, and each other agreement executed in connection therewith.

“**EXIM Eligible Receivables**” means Eligible Export-Related Accounts Receivable as defined in the Borrower Agreement.

“**EXIM Facility Fee**” means a fee equal to one and three-quarters percent (1.75%) of the EXIM Credit Limit due upon the Closing Date and each anniversary thereof so long as any Advances are outstanding or available hereunder.

“**EXIM Guarantee**” means the Master Guaranty Agreement executed by EXIM Bank in favor of Lender.

“**EXIM Line of Credit**” means the revolving line of credit under which Borrower may request Lender to issue Advances with respect to EXIM Eligible Receivables up to the EXIM Credit Limit, as specified in Section 1.1 hereof.

“**EXIM Overadvance**” means at any time an amount equal to the amount (if any) by which the total amount of the outstanding Advances with respect to EXIM Eligible Receivables exceeds the lesser of the EXIM Credit Limit or the EXIM Borrowing Base.

“**Event of Default**” has the meaning set forth in Section 7.1.

“**Finance Charge**” means an interest amount equal to the Finance Charge Percentage of the ending daily Account Balance for the relevant period.

“**Finance Charge Percentage**” means a floating rate per year equal to (i) the Prime Rate plus one and one-half percentage points (1.50%) with respect to Advances made under the Domestic Line of Credit, and (ii) the Prime Rate plus one and one-half percentage points (1.50%) with respect to Advances made under the EXIM Line of Credit, and, in each case, plus an additional five percentage points (5.00%) during any period that an Event of Default has occurred and is continuing.

“**GAAP**” means generally accepted accounting principles consistently applied and used consistently with prior practices.

“**Governmental Approval**” is any consent, authorization, approval, order, license, franchise, permit, certificate, accreditation, registration, filing or notice, of, issued by, from or to, or other act by or in respect of, any Governmental Authority.

“**Governmental Authority**” is any nation or government, any state or other political subdivision thereof, any agency, authority, instrumentality, regulatory body, court, central bank or other entity exercising executive, legislative, judicial, taxing, regulatory or administrative functions of or pertaining to government, any securities exchange and any self-regulatory organization.

“**International Sublimit**” means \$500,000.

“**Lender**” means WESTERN ALLIANCE BANK, an Arizona corporation, and its successors and assigns.

“**Letter of Credit**” has the meaning set forth in Section 1.8.

“**Letter of Credit Obligations**” means, at any time, the sum of, without duplication, (i) the maximum amount available to be drawn on all outstanding Letters of Credit issued by Lender or by Lender’s Affiliate and (ii) the aggregate amount of all amounts drawn and unreimbursed with respect to Letters of Credit issued by Lender or by Lender’s Affiliate.

“**Lockbox**” is defined in the Lockbox Agreement.

“**Lockbox Agreement**” is defined in Section 1.4(a).

“**Material Adverse Change**” means a material adverse change in Borrower’s (or any guarantor’s) business condition (financial or otherwise), operations, properties or prospects, or ability to repay the credit.

“**Maturity Date**” means two years from the Closing Date or such earlier date as Lender shall have declared the Obligations immediately due and payable pursuant to Section 7.2.

“**Month End**” means the last calendar day of each month.

“**Obligations**” means all liabilities and obligations of Borrower to Lender of any kind or nature, present or future, arising under or in connection with this Agreement or under any other document, instrument or agreement, whether or not evidenced by any note, guarantee or other instrument, whether arising on account or by overdraft, whether direct or indirect (including those acquired by assignment) absolute or contingent, primary or secondary, due or to become due, now owing or hereafter arising, and however acquired; including, without limitation, all Advances, Finance Charges, fees, interest, expenses, professional fees and attorneys’ fees.

“**Overadvance**” means a Domestic Overadvance or an EXIM Overadvance.

“**Permitted Indebtedness**” means:

- (a) Indebtedness under this Agreement or that is otherwise owed to Lender.

- (b) Indebtedness existing on the Closing Date and specifically disclosed on a schedule to this Agreement.
- (c) Purchase money indebtedness (including capital leases) incurred to acquire capital assets in ordinary course of business and not exceeding \$25,000 in total principal amount at any time outstanding.
- (d) Other indebtedness in an aggregate amount not to exceed \$25,000 at any time outstanding; provided that such indebtedness is junior in priority (if secured) to the Obligations and provided that the incurrence of such Indebtedness does not otherwise cause an Event of Default hereunder.
- (e) Indebtedness incurred in the refinancing of any indebtedness set forth in (a) through (d) above, provided that the principal amount thereof is not increased or the terms thereof are not modified to impose more burdensome terms upon Borrower.
- (f) Subordinated Debt.

“Permitted Investment” means:

- (a) Investments existing on the Closing Date and specifically disclosed on a schedule to this Agreement.
- (b) Cash Equivalents and Lender’s money market accounts.

“Permitted Liens” means the following but only with respect to property not consisting of Receivables:

- (a) Liens securing any of the indebtedness described in clauses (a) through (d) of the definition of Permitted Indebtedness.
- (b) Liens for taxes, fees, assessments or other governmental charges or levies, either not delinquent or being contested in good faith by appropriate proceedings, provided the same have no priority over any of Lender’s security interests.
- (c) Liens incurred in connection with the extension, renewal or refinancing of the indebtedness described in clause (e) of the definition of Permitted Indebtedness, provided that any extension, renewal or replacement lien shall be limited to the property encumbered by the existing lien and the principal amount of the indebtedness being extended, renewed or refinanced does not increase.
- (d) Liens securing Subordinated Debt.

“Person” shall mean any individual, sole proprietorship, partnership, limited liability partnership, joint venture, trust, unincorporated organization, association, corporation, limited liability company, institution, public benefit corporation, entity or government (whether national, federal, provincial, state, county, city, municipal or otherwise, including any instrumentality, division, agency, body or department thereof), and shall include such Person's successors and assigns.

“Prime Rate” means the greater of four and one-half percent (4.50%) per year or the Prime Rate published in the Money Rates section of the Western Edition of The Wall Street Journal, or such other rate of interest publicly announced from time to time by Lender as its Prime Rate. Lender may price loans to its customers at, above, or below the Prime Rate. Any change in the Prime Rate shall take effect at the opening of business on the day specified in the public announcement of a change in the Prime Rate.

“Receivable Amount” means as to any Receivable, the amount due from the Account Debtor after deducting all discounts, credits, offsets, payments or other deductions of any nature whatsoever, whether or not claimed by the Account Debtor.

“Receivables” means Borrower’s rights to payment arising in the ordinary course of Borrower’s business, including accounts, chattel paper, instruments, contract rights, documents, general intangibles, letters of credit, drafts, and bankers acceptances.

“Requirement of Law” is as to any Person, the organizational or governing documents of such Person, and any law (statutory or common), treaty, rule or regulation or determination of an arbitrator or a court or other Governmental Authority, in each case applicable to or binding upon such Person or any of its property or to which such Person or any of its property is subject.

“Subordinated Debt” means indebtedness of Borrower that is expressly subordinated to the indebtedness of Borrower owed to Lender pursuant to a subordination agreement satisfactory in form and substance to Lender.

“Subsidiary” is, as to any Person, a corporation, partnership, limited liability company or other entity of which shares of stock or other ownership interests having ordinary voting power (other than stock or such other ownership interests having such power only by reason of the happening of a contingency) to elect a majority of the board of directors or other managers of such corporation, partnership or other entity are at the time owned, or the management of which is otherwise controlled, directly or indirectly through one or more intermediaries, or both, by such Person. Unless the context otherwise requires, each reference to a Subsidiary herein shall be a reference to a Subsidiary of Borrower.

“UCC” means the Arizona Uniform Commercial Code, as amended or supplemented from time to time.

12.2 Construction:

- (a) In this Agreement: (i) references to the plural include the singular and to the singular include the plural; (ii) references to any gender include any other gender; (iii) the terms “include” and “including” are not limiting; (iv) the term “or” has the inclusive meaning represented by the phrase “and/or;” (v) unless otherwise specified, section and subsection references are to this Agreement, and (vi) any reference to any statute, law, or regulation shall include all amendments thereto and revisions thereof.
- (b) Neither this Agreement nor any uncertainty or ambiguity herein shall be construed or resolved using any presumption against either Borrower or Lender, whether under any rule of construction or otherwise. On the contrary, this Agreement has been reviewed by each party hereto and their respective counsel. In case of any ambiguity or uncertainty, this Agreement shall be construed and interpreted according to the ordinary meaning of the words used to accomplish fairly the purposes and intentions of all parties hereto.

- (c) Titles and section headings used in this Agreement are for convenience only and shall not be used in interpreting this Agreement.

- 13. JURY TRIAL WAIVER.** THE UNDERSIGNED ACKNOWLEDGE THAT THE RIGHT TO TRIAL BY JURY IS A CONSTITUTIONAL ONE, BUT THAT IT MAY BE WAIVED UNDER CERTAIN CIRCUMSTANCES. TO THE EXTENT PERMITTED BY LAW, EACH PARTY, AFTER CONSULTING (OR HAVING HAD THE OPPORTUNITY TO CONSULT) WITH COUNSEL OF ITS, HIS OR HER CHOICE, KNOWINGLY AND VOLUNTARILY, AND FOR THE MUTUAL BENEFIT OF ALL PARTIES, WAIVES ANY RIGHT TO TRIAL BY JURY IN THE EVENT OF LITIGATION ARISING OUT OF OR RELATED TO THIS AGREEMENT OR ANY OTHER DOCUMENT, INSTRUMENT OR AGREEMENT BETWEEN THE UNDERSIGNED PARTIES.
- 14. RESERVED.**
- 15. EXECUTION, EFFECTIVENESS, SURVIVAL .** This Agreement may be executed in counterparts (and by different parties hereto in different counterparts), each of which shall constitute an original, but all of which when taken together shall constitute a single contract. This Agreement and the other documents executed in connection herewith constitute the entire contract among the parties relating to the subject matter hereof and supersede any and all previous agreements and understandings, oral or written, relating to the subject matter hereof. Delivery of an executed counterpart of a signature page of this Agreement by telecopy shall be effective as delivery of a manually executed counterpart of this Agreement. This Agreement shall become effective upon the execution and delivery hereof by Borrower and Lender and shall continue in full force and effect until the Maturity Date and thereafter so long as any Obligations remain outstanding hereunder. Lender reserves the right to issue press releases, advertisements, and other promotional materials describing any successful outcome of services provided on Borrower's behalf. Borrower agrees that Lender shall have the right to identify Borrower by name in those materials.
- 16. OTHER AGREEMENTS.** Any security agreements, liens and/or security interests securing payment of any obligations of Borrower owing to Lender or its Affiliates also secure the Obligations and are valid and subsisting and are not adversely affected by execution of this Agreement. An Event of Default under this Agreement constitutes a default under other outstanding agreements between Borrower and Lender or its Affiliates.
- 17. BORROWER LIABILITY.** Any Borrower may, acting singly, request credit extensions hereunder. Each Borrower hereby appoints the other as agent for itself for all purposes hereunder, including with respect to requesting credit extensions hereunder. Each Borrower hereunder shall be jointly and severally obligated to repay all Obligations, including, without limitation, all credit extensions made hereunder, regardless of which Borrower actually receives said credit extensions, as if each Borrower hereunder directly received all credit extensions. Each Borrower waives (a) any suretyship defenses available to it under the UCC or any other applicable law, and (b) any right to require Lender to: (i) proceed against any Borrower or any other person; (ii) proceed against or exhaust any security; or (iii) pursue any other remedy. Lender may exercise or not exercise any right or remedy it has against any Borrower or any security it holds (including the right to foreclose by judicial or non-judicial sale) without affecting any Borrower's liability.

Notwithstanding any other provision of this Agreement or other related document, each Borrower irrevocably waives all rights that it may have at law or in equity (including, without limitation, any law subrogating Borrower to the rights of Lender under this Agreement) to seek contribution, indemnification or any other form of reimbursement from any other Borrower, or any other Person now

or hereafter primarily or secondarily liable for any of the Obligations, for any payment made by Borrower with respect to the Obligations in connection with this Agreement or otherwise and all rights that it might have to benefit from, or to participate in, any security for the Obligations as a result of any payment made by Borrower with respect to the Obligations in connection with this Agreement or otherwise. Any agreement providing for indemnification, reimbursement or any other arrangement prohibited under this Section shall be null and void. If any payment is made to a Borrower in contravention of this Section, such Borrower shall hold such payment in trust for Lender and such payment shall be promptly delivered to Lender for application to the Obligations, whether matured or unmatured.

- 18. REVIVAL AND REINSTATEMENT OF OBLIGATIONS.** If the incurrence or payment of the Obligations by Borrower or any guarantor, or the transfer to Lender of any property should for any reason subsequently be asserted, or declared, to be void or voidable under any state or federal law relating to creditors' rights, including provisions of the United States Bankruptcy Code relating to fraudulent conveyances, preferences, or other voidable or recoverable payments of money or transfers of property (each, a "Voidable Transfer"), and if Lender is required to repay or restore, in whole or in part, any such Voidable Transfer, or elects to do so upon the reasonable advice of its counsel, then, as to any such Voidable Transfer, or the amount thereof that Lender is required or elects to repay or restore, and as to all reasonable costs, expenses, and reasonable attorneys' fees of Lender related thereto, the liability of Borrower and such guarantor automatically shall be revived, reinstated, and restored and shall exist as though such Voidable Transfer had never been made.
- 19. PATRIOT ACT NOTIFICATION.** Lender hereby notifies Borrower that pursuant to the requirements of the USA Patriot Act, Title III of Pub. L. 107-56, signed into law October 26, 2001 ("Patriot Act"), Lender is required to obtain, verify and record information that identifies Borrower, which information includes the names and addresses of Borrower and other information that will allow Lender to identify Borrower in accordance with the Patriot Act.
- 20. NOTICE OF FINAL AGREEMENT.** BY SIGNING THIS DOCUMENT EACH PARTY REPRESENTS AND AGREES THAT: (A) THIS WRITTEN AGREEMENT REPRESENTS THE FINAL AGREEMENT BETWEEN THE PARTIES, (B) THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN THE PARTIES, AND (C) THIS WRITTEN AGREEMENT MAY NOT BE CONTRADICTED BY EVIDENCE OF ANY PRIOR, CONTEMPORANEOUS, OR SUBSEQUENT ORAL AGREEMENTS OR UNDERSTANDINGS OF THE PARTIES.

[Signature pages follow.]

IN WITNESS WHEREOF, Borrower and Lender have executed this Agreement on the day and year above written.

BORROWER:

BIOLASE, INC.
By /s/ John R. Beaver
Name: John R. Beaver
Title: SVP and Chief Financial Officer

Address for Notices:

Biolase, Inc.
4 Cromwell
Irvine, CA 92618

BL ACQUISITION CORP.

By /s/ John R. Beaver
Name: John R. Beaver
Title: SVP and Chief Financial Officer

Address for Notices:

BL Acquisition Corp.
4 Cromwell
Irvine, CA 92618

BL ACQUISITION II INC.

By /s/ John R. Beaver
Name: John R. Beaver
Title: SVP and Chief Financial Officer

Address for Notices:

BL Acquisition II Inc.
4 Cromwell
Irvine, CA 92618

LENDER:

WESTERN ALLIANCE BANK, AN
ARIZONA CORPORATION

By /s/ Victor Le
Name: Victor Le
Title: Vice President

Address for Notices:

Bridge Bank
a division of Western Alliance Bank, an
Arizona corporation
3200 Park Center Drive, Suite 350
Costa Mesa, CA 92626

**EXPORT-IMPORT BANK OF THE UNITED STATES WORKING CAPITAL
GUARANTEE PROGRAM**

BORROWER AGREEMENT

Ex-Im Bank 12/31/05

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**EXPORT-IMPORT BANK OF THE UNITED STATES WORKING
CAPITAL GUARANTEE PROGRAM BORROWER
AGREEMENT**

THIS BORROWER AGREEMENT (this "Agreement") is made and entered into by the entity identified as Borrower on the signature page hereof ("Borrower") in favor of the Export-Import Bank of the United States ("Ex-Im Bank") and the institution identified as Lender on the signature page hereof ("Lender").

RECITALS

Borrower has requested that Lender establish a Loan Facility in favor of Borrower for the purposes of providing Borrower with working capital to finance the manufacture, production or purchase and subsequent export sale of Items.

Lender and Borrower expect that Ex-Im Bank will provide a guarantee to Lender regarding this Loan Facility subject to the terms and conditions of the Master Guarantee Agreement, a Loan Authorization Agreement, and to the extent applicable, the Delegated Authority Letter Agreement or Fast Track Lender Agreement.

Lender and Ex-Im Bank have requested that Borrower execute this Agreement as a condition precedent to Lender establishing the Loan Facility and Ex-Im Bank providing the guarantee.

NOW, THEREFORE, Borrower hereby agrees as follows:

**ARTICLE I
DEFINITIONS**

1.01 Definition of Terms. As used in this Agreement, including the Recitals to this Agreement and the Loan Authorization Agreement, the following terms shall have the following meanings:

"Accounts Receivable" shall mean all of Borrower's now owned or hereafter acquired (a) "accounts" (as such term is defined in the UCC), other receivables, book debts and other forms of obligations, whether arising out of goods sold or services rendered or from any other transaction; (b) rights in, to and under all purchase orders or receipts for goods or services; (c) rights to any goods represented or purported to be represented by any of the foregoing (including unpaid sellers' rights of rescission, replevin, reclamation and stoppage in transit and rights to returned, reclaimed or repossessed goods); (d) moneys due or to become due to such Borrower under all purchase orders and contracts (which includes Export Orders) for the sale of goods or the performance of services or both by Borrower (whether or not yet earned by performance on the part of Borrower), including the proceeds of the foregoing; (e) any notes, drafts, letters of credit, insurance proceeds or other instruments, documents and writings evidencing or supporting the foregoing; and (f) all collateral security and guarantees of any kind given by any other Person with respect to any of the foregoing.

“Accounts Receivable Aging Report” shall mean a report detailing the Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable for a Loan Facility, and the applicable terms for the relevant time period; in the case of Indirect Exports, such report shall indicate the portion of such Accounts Receivables corresponding to Indirect Exports.

"Advance Rate" shall mean, with respect to a Loan Facility, the rate specified in Section 5.C. of the Loan Authorization Agreement for each category of Primary Collateral except for Export-Related General Intangibles and Other Collateral. Unless otherwise set forth in writing by Ex-Im Bank, in no event shall the Advance Rate exceed (i) ninety percent (90%) for Eligible Export-Related Accounts Receivable, (ii) seventy five percent (75%) for Eligible Export-Related Inventory, (iii) seventy percent (70%) for Eligible Export-Related Overseas Accounts Receivable or (iv) sixty percent (60%) for Eligible Export-Related Overseas Inventory and (v) twenty five percent (25%) for Retainage Accounts Receivable.

“Affiliated Foreign Person” shall have the meaning set forth in Section 2.15.

"Business Day" shall mean any day on which the Federal Reserve Bank of New York is open for business.

"Buyer" shall mean a Person that has entered into one or more Export Orders with Borrower or who is an obligor on Export-Related Accounts Receivable or Export-Related Overseas Accounts Receivable.

“Capital Good” shall mean a capital good (e.g., manufacturing equipment, licensing agreements) that will establish or expand foreign production capacity of an exportable good.

"Collateral" shall mean all real and personal property and interest in real and personal property in or upon which Lender has been, or shall be, granted a Lien as security for the payment of all the Loan Facility Obligations and all products and proceeds (cash and non-cash) thereof.

"Commercial Letters of Credit" shall mean those letters of credit subject to the UCP payable in Dollars and issued or caused to be issued by Lender on behalf of Borrower under a Loan Facility for the benefit of a supplier(s) of Borrower in connection with Borrower's purchase of goods or services from the supplier in support of the export of the Items.

"Country Limitation Schedule" shall mean the schedule published from time to time by Ex-Im Bank setting forth on a country by country basis whether and under what conditions ExIm Bank will provide coverage for the financing of export transactions to countries listed therein.

“Credit Accommodation Amount” shall mean, the sum of (a) the aggregate outstanding amount of Disbursements and (b) the aggregate outstanding Letter of Credit Obligations, which sum may not exceed the Maximum Amount.

"Credit Accommodations" shall mean, collectively, Disbursements and Letter of Credit Obligations.

"Debarment Regulations" shall mean, collectively, (a) the Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 53 Fed. Reg. 19204 (May 26, 1988), (b) Subpart 9.4 (Debarment, Suspension, and Ineligibility) of the Federal Acquisition Regulations, 48 C.F.R. 9.400-9.409 and (c) the revised Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 60 Fed. Reg. 33037 (June 26, 1995).

"Delegated Authority Letter Agreement" shall mean the Delegated Authority Letter Agreement, if any, between Ex-Im Bank and Lender.

"Disbursement" shall mean, collectively, (a) an advance of a working capital loan from Lender to Borrower under the Loan Facility, and (b) an advance to fund a drawing under a Letter of Credit issued or caused to be issued by Lender for the account of Borrower under the Loan Facility.

"Dollars" or "\$" shall mean the lawful currency of the United States.

"Economic Impact Approval" shall mean a written approval issued by Ex-Im Bank stating the conditions under which a Capital Good may be included as an Item in a Loan Facility consistent with Ex-Im Bank's economic impact procedures (or other mechanism for making this determination that Ex-Im Bank notifies Lender of in writing).

"Economic Impact Certification" shall have the meaning set forth in Section 2.14(b).

"Effective Date" shall mean the date on which (a) all of the Loan Documents have been executed by Lender, Borrower and, if applicable, Ex-Im Bank and (b) all of the conditions to the making of the initial Credit Accommodations under the Loan Documents or any amendments thereto have been satisfied.

"Eligible Export-Related Accounts Receivable" shall mean Export-Related Accounts Receivable which are acceptable to Lender and which are deemed to be eligible pursuant to the Loan Documents, but in no event shall Eligible Export-Related Accounts Receivable include any Account Receivable:

- (a) that does not arise from the sale of Items in the ordinary course of Borrower's business;
- (b) that is not subject to a valid, perfected first priority Lien in favor of Lender;
- (c) as to which any covenant, representation or warranty contained in the Loan Documents with respect to such Account Receivable has been breached;
- (d) that is not owned by Borrower or is subject to any right, claim or interest of another Person other than the Lien in favor of Lender;
- (e) with respect to which an invoice has not been sent;
- (f) that arises from the sale of defense articles or defense services;

- (g) that arises from the sale of Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities unless with Ex-Im Bank's prior written consent;
- (h) that is due and payable from a Buyer located in a country with which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;
- (i) that does not comply with the requirements of the Country Limitation Schedule;
- (j) that is due and payable more than one hundred eighty (180) days from the date of the invoice;
- (k) that is not paid within sixty (60) calendar days from its original due date, unless it is insured through Ex-Im Bank export credit insurance for comprehensive commercial and political risk, or through Ex-Im Bank approved private insurers for comparable coverage, in which case it is not paid within ninety (90) calendar days from its due date;
- (l) of a Buyer for whom fifty percent (50%) or more of the Accounts Receivable of such Buyer do not satisfy the requirements of subclauses (j) and (k) above;
- (m) that arises from a sale of goods to or performance of services for an employee of Borrower, a stockholder of Borrower, a subsidiary of Borrower, a Person with a controlling interest in Borrower or a Person which shares common controlling ownership with Borrower;
- (n) that is backed by a letter of credit unless the Items covered by the subject letter of credit have been shipped;
- (o) that Lender or Ex-Im Bank, in its reasonable judgment, deems uncollectible for any reason;
- (p) that is due and payable in a currency other than Dollars, except as may be approved in writing by Ex-Im Bank;
- (q) that is due and payable from a military Buyer, except as may be approved in writing by Ex-Im Bank;
- (r) that does not comply with the terms of sale set forth in Section 7 of the Loan Authorization Agreement;
- (s) that is due and payable from a Buyer who (i) applies for, suffers, or consents to the appointment of, or the taking of possession by, a receiver, custodian, trustee or liquidator of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have

dismissed, any petition which is filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;

(t) that arises from a bill-and-hold, guaranteed sale, sale-and-return, sale on approval, consignment or any other repurchase or return basis or is evidenced by chattel paper;

(u) for which the Items giving rise to such Accounts Receivable have not been shipped to the Buyer or when the Items are services, such services have not been performed or when the Export Order specifies a timing for invoicing the Items other than shipment or performance and the Items have not been invoiced in accordance with such terms of the Export Order, or the Accounts Receivable otherwise do not represent a final sale;

(v) that is subject to any offset, deduction, defense, dispute, or counterclaim or the Buyer is also a creditor or supplier of Borrower or the Account Receivable is contingent in any respect or for any reason;

(w) for which Borrower has made any agreement with the Buyer for any deduction therefrom, except for discounts or allowances made in the ordinary course of business for prompt payment, all of which discounts or allowances are reflected in the calculation of the face value of each respective invoice related thereto;

(x) for which any of the Items giving rise to such Account Receivable have been returned, rejected or repossessed;

(y) that is included as an eligible receivable under any other credit facility to which Borrower is a party;

(z) any of the Items giving rise to such Accounts Receivable are Capital Goods, unless the transaction is in accordance with Section 2.14;

(aa) that is due and payable from a Buyer that is, or is located in, the United States; provided however, that this subsection (aa) shall not preclude an Export-Related Accounts Receivable arising from the sale of Items to foreign contractors or subcontractors providing services to a United States Embassy or the United States Military located overseas from being deemed an Eligible Export-Related Accounts Receivable; or

(bb) that arises from the sale of Items that do not meet the U.S. Content requirements in accordance with Section 2.01(b) (ii).

"Eligible Export-Related Inventory" shall mean Export-Related Inventory which is acceptable to Lender and which is deemed to be eligible pursuant to the Loan Documents, but in no event shall Eligible Export-Related Inventory include any Inventory:

(a) that is not subject to a valid, perfected first priority Lien in favor of Lender;

(b) that is located at an address that has not been disclosed to Lender in writing;

- (c) that is placed by Borrower on consignment or held by Borrower on consignment from another Person;
- (d) that is in the possession of a processor or bailee, or located on premises leased or subleased to Borrower, or on premises subject to a mortgage in favor of a Person other than Lender, unless such processor or bailee or mortgagee or the lessor or sublessor of such premises, as the case may be, has executed and delivered all documentation which Lender shall require to evidence the subordination or other limitation or extinguishment of such Person's rights with respect to such Inventory and Lender's right to gain access thereto;
- (e) that is produced in violation of the Fair Labor Standards Act or subject to the "hot goods" provisions contained in 29 U.S.C. §215 or any successor statute or section;
- (f) as to which any covenant, representation or warranty with respect to such Inventory contained in the Loan Documents has been breached;
- (g) that is not located in the United States unless expressly permitted by Lender, on terms acceptable to Lender;
- (h) that is an Item or is to be incorporated into Items that do not meet U.S. Content requirements in accordance with Section 2.01(b)(ii);
- (i) that is demonstration Inventory;
- (j) that consists of proprietary software (i.e. software designed solely for Borrower's internal use and not intended for resale);
- (k) that is damaged, obsolete, returned, defective, recalled or unfit for further processing;
- (l) that has been previously exported from the United States;
- (m) that constitutes, or will be incorporated into Items that constitute, defense articles or defense services;
- (n) that is an Item or will be incorporated into Items that will be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities unless with Ex-Im Bank's prior written consent;
- (o) that is an Item or is to be incorporated into Items destined for shipment to a country as to which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;
- (p) that is an Item or is to be incorporated into Items destined for shipment to a Buyer located in a country in which Ex-Im Bank coverage is not available for commercial reasons as designated in the Country Limitation Schedule, unless and only to the extent that such Items are to be sold to such country on terms of a letter of credit confirmed by a bank acceptable to Ex-Im Bank;

(q) that constitutes, or is to be incorporated into, Items whose sale would result in an Accounts Receivable which would not be an Eligible Export-Related Accounts Receivable;

(r) that is included as eligible inventory under any other credit facility to which Borrower is a party; or

(s) that is, or is to be incorporated into, an Item that is a Capital Good, unless the transaction is in accordance with Section 2.14.

"Eligible Export-Related Overseas Accounts Receivable" shall mean Export-Related Overseas Accounts Receivable which are acceptable to Lender and which are deemed to be eligible pursuant to the Loan Documents but in no event shall include the Accounts Receivable (a) through (bb) excluded from the definition of Eligible Export-Related Accounts Receivable.

"Eligible Export-Related Overseas Inventory" shall mean Export-Related Overseas Inventory which is acceptable to Lender and which is deemed to be eligible pursuant to the Loan Documents, but in no event shall include the Inventory (a) through (r) excluded from the definition of Eligible Export-Related Inventory.

"Eligible Person" shall mean a sole proprietorship, partnership, limited liability partnership, corporation or limited liability company which (a) is domiciled, organized or formed, as the case may be, in the United States, whether or not such entity is owned by a foreign national or foreign entity; (b) is in good standing in the state of its formation or otherwise authorized to conduct business in the United States; (c) is not currently suspended or debarred from doing business with the United States government or any instrumentality, division, agency or department thereof; (d) exports or plans to export Items; (e) operates and has operated as a going concern for at least one (1) year; (f) has a positive tangible net worth determined in accordance with GAAP; and (g) has revenue generating operations relating to its core business activities for at least one year. An Affiliated Foreign Person that meets all of the requirements of the foregoing definition of Eligible Person other than subclause (a) thereof shall be deemed to be an Eligible Person

"ERISA" shall mean the Employee Retirement Income Security Act of 1974 and the rules and regulations promulgated thereunder

"Export Order" shall mean a documented purchase order or contract evidencing a Buyer's agreement to purchase the Items from Borrower for export from the United States, which documentation shall include written information that is necessary to confirm such purchase order or contract, including identification of the Items, the name of the Buyer, the country of destination, contact information for the Buyer and the total amount of the purchase order or contract; in the case of Indirect Exports, such documentation shall further include a copy of the written purchase order or contract from a foreign purchaser or other documentation clearly evidencing a foreign purchaser's agreement to purchase the Items.

"Export-Related Accounts Receivable" shall mean those Accounts Receivable arising from the sale of Items which are due and payable to Borrower in the United States.

"Export-Related Accounts Receivable Value" shall mean, at the date of determination thereof, the aggregate face amount of Eligible Export-Related Accounts Receivable less taxes, discounts, credits, allowances and Retainages, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Export-Related Borrowing Base" shall mean, at the date of determination thereof, the sum of (a) (if Lender elects to include) the Export-Related Inventory Value or Export-Related Historical Inventory Value multiplied by the Advance Rate applicable to Eligible Export-Related Inventory set forth in Section 5.B.(1.) of the Loan Authorization Agreement, plus (b) the Export-Related Accounts Receivable Value multiplied by the Advance Rate applicable to Eligible Export-Related Accounts Receivable set forth in Section 5.B.(2.) of the Loan Authorization Agreement, plus (c) if permitted by Ex-Im Bank in writing, the Retainage Value multiplied by the Advance Rate applicable to Retainages set forth in Section 5.B.(3.) of the Loan Authorization Agreement, plus (d) the Other Assets set forth in Section 5.B.(4.) of the Loan Authorization Agreement multiplied by the Advance Rate agreed to in writing by Ex-Im Bank, plus (e) if permitted by Ex-Im Bank in writing, the Export-Related Overseas Accounts Receivable Value multiplied by the Advance Rate applicable to Eligible Export-Related Overseas Accounts Receivable set forth in Section 5.B.(5.) of the Loan Authorization Agreement, plus (f) if permitted by Ex-Im Bank in writing, the Export-Related Overseas Inventory Value multiplied by the Advance Rate applicable to Eligible Export-Related Overseas Inventory set forth in Section 5.B.(6.) of the Loan Authorization Agreement, less (g) the amounts required to be reserved pursuant to Sections 4.12 and 4.13 of this Agreement for each outstanding Letter of Credit, less (h) such reserves and in such amounts deemed necessary and proper by Lender from time to time.

"Export-Related Borrowing Base Certificate" shall mean a certificate in the form provided or approved by Lender, executed by Borrower and delivered to Lender pursuant to the Loan Documents detailing the Export-Related Borrowing Base supporting the Credit Accommodations which reflects, to the extent included in the Export-Related Borrowing Base, Export-Related Accounts Receivable, Eligible Export-Related Accounts Receivable, Export-Related Inventory, Eligible Export-Related Inventory, Export-Related Overseas Accounts Receivable, Eligible Export-Related Accounts Receivable, Export-Related Overseas Inventory and Eligible Export-Related Overseas Inventory balances that have been reconciled with Borrower's general ledger, Accounts Receivable Aging Report and Inventory schedule.

"Export-Related General Intangibles" shall mean the Pro Rata Percentage of General Intangibles determined as of the earlier of: (i) the date such General Intangibles are liquidated and (ii) the date Borrower fails to pay when due any outstanding amount of principal or accrued interest payable under the Loan Documents that becomes the basis for a Payment Default on which a Claim is filed.

"Export-Related Historical Inventory Value" shall mean with respect to a Borrower, the relevant Export-Related Sales Ratio multiplied by the lowest of (i) the cost of such Borrower's Inventory as determined in accordance with GAAP, or (ii) the market value of such Borrower's Inventory as determined in accordance with GAAP or (iii) the appraised or orderly liquidation value of such Borrower's Inventory, if Lender has loans and financial accommodations to such Borrower for which it conducts (or contracts for the performance of) such an appraised or orderly liquidation value.

"Export-Related Inventory" shall mean the Inventory of Borrower located in the United States that has been purchased, manufactured or otherwise acquired by Borrower for sale or resale as Items, or to be incorporated into Items to be sold or resold pursuant to Export Orders.

"Export-Related Inventory Value" shall mean, at the date of determination thereof, the lowest of (i) the cost of Eligible Exported-Related Inventory as determined in accordance with GAAP, or (ii) the market value of Eligible Export-Related Inventory as determined in accordance with GAAP or (iii) the lower of the appraised market value or orderly liquidation value of the Eligible Export-Related Inventory, if Lender has other loans and financial accommodations to a Borrower for which it conducts (or contracts for the performance of) such an appraised or orderly liquidation value.

"Export-Related Overseas Accounts Receivable" shall mean those Accounts Receivable arising from the sale of Items which are due and payable outside of the United States either to a Borrower or an Affiliated Foreign Person.

"Export-Related Overseas Accounts Receivable Value" shall mean, with respect to a Loan Facility, at the date of determination thereof, the aggregate face amount of Eligible Export-Related Overseas Accounts Receivable less taxes, discounts, credits, allowances and Retainages, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Export-Related Overseas Inventory" shall mean the Inventory of Borrower located outside of the United States that has been purchased, manufactured or otherwise acquired by such Borrower for sale or resale as Items, or to be incorporated into Items to be sold or resold pursuant to Export Orders.

"Export-Related Overseas Inventory Value" shall mean, at the date of determination thereof, the lowest of (i) the cost of Eligible Export-Related Overseas Inventory as determined in accordance with GAAP, (ii) the market value of Eligible Export-Related Overseas Inventory as determined in accordance with GAAP or (iii) the appraised or orderly liquidation value of the Eligible Export-Related Overseas Inventory, if Lender has other loans and financial accommodations to Borrower or an Affiliated Foreign Person for which it conducts (or contracts for the performance of) such a appraised or orderly liquidation.

"Export-Related Sales Ratio" shall mean with respect to a Borrower, the percentage of such Borrower's total sales revenue derived from the sale of Eligible Export-Related Inventory over a rolling twelve-month period ending no more than ninety (90) days prior to the date of the relevant Export-Related Borrowing Base Certificate

"Extension" shall mean, with respect to a Loan Facility, an amendment to the Loan Authorization Agreement extending the Final Disbursement Date on the same terms and conditions as the Loan Facility for an aggregate period not to exceed one hundred and twenty (120) days beyond the original Final Disbursement Date, either as agreed to in writing by Ex-Im Bank or, in the case of Delegated Authority, as notified by Lender to Ex-Im Bank pursuant to its authority under the Delegated Authority Letter Agreement.

“Fast Track Lender Agreement” shall mean the Fast Track Lender Agreement, if any, between Ex-Im Bank and Lender.

"Final Disbursement Date" shall mean the last date on which Lender may make a Disbursement set forth in Section 10 of the Loan Authorization Agreement (including as amended by an Extension) or, if such date is not a Business Day, the next succeeding Business Day; provided, however, to the extent that Lender has not received cash collateral in the amount of the Letter of Credit Obligations or an equivalent full indemnity from Borrower or Guarantor, as applicable, with respect to Letter of Credit Obligations outstanding on the Final Disbursement Date, the Final Disbursement Date with respect to an advance to fund a drawing under such Letter of Credit shall be no later than thirty (30) days after any such drawing which may be no later than the expiry date of the Letter of Credit related thereto.

"GAAP" shall mean the generally accepted accounting principles issued in the United States.

"General Intangibles" shall mean all intellectual property and other "general intangibles" (as such term is defined in the UCC).

"Guarantor" shall mean any Person which is identified in Section 3 of the Loan Authorization Agreement who shall guarantee (jointly and severally if more than one) the payment and performance of all or a portion of the Loan Facility Obligations.

"Guarantee Agreement" shall mean a valid and enforceable agreement of guarantee executed by each Guarantor in favor of Lender.

"Indirect Exports" shall mean finished goods or services that are sold by a Borrower to a Buyer located in the United States, are intended for export from the United States, and are identified in Section 4.A.(2.) of the Loan Authorization Agreement.

"Inventory" shall mean all "inventory" (as such term is defined in the UCC), now or hereafter owned or acquired by Borrower, wherever located, including all inventory, merchandise, goods and other personal property which are held by or on behalf of Borrower for sale or lease or are furnished or are to be furnished under a contract of service or which constitute raw materials, work in process or materials used or consumed or to be used or consumed in Borrower's business or in the processing, production, packaging, promotion, delivery or shipping of the same, including other supplies.

"ISP" shall mean the International Standby Practices-ISP98, International Chamber of Commerce Publication No. 590 and any amendments and revisions thereof.

"Issuing Bank" shall mean the bank that issues a Letter of Credit, which bank is Lender itself or a bank that Lender has caused to issue a Letter of Credit by way of a guarantee or reimbursement obligation.

"Items" shall mean the finished goods or services which are intended for export from the United States, either directly or as an Indirect Export, meet the U.S. Content requirements in

accordance with Section 2.01(b)(ii) of this Agreement and are specified in Section 4.A. of the Loan Authorization Agreement.

"Letter of Credit" shall mean a Commercial Letter of Credit or a Standby Letter of Credit.

"Letter of Credit Obligations" shall mean all undrawn amounts of outstanding obligations incurred by Lender, whether direct or indirect, contingent or otherwise, due or not due, in connection with the issuance or guarantee by Lender or Issuing Bank of Letters of Credit.

"Lien" shall mean any mortgage, security deed or deed of trust, pledge, hypothecation, assignment, deposit arrangement, lien, charge, claim, security interest, security title, easement or encumbrance, or preference, priority or other security agreement or preferential arrangement of any kind or nature whatsoever (including any lease or title retention agreement, any financing lease having substantially the same economic effect as any of the foregoing, and the filing of, or agreement to give, any financing statement perfecting a security interest under the UCC or comparable law of any jurisdiction) by which property is encumbered or otherwise charged.

"Loan Agreement" shall mean a valid and enforceable agreement between Lender and a Borrower setting forth, with respect to each Loan Facility, the terms and conditions of such Loan Facility.

"Loan Authorization Agreement" shall mean, as applicable, the duly executed Loan Authorization Agreement, Fast Track Loan Authorization Agreement, or the Loan Authorization Notice, setting forth certain terms and conditions of each Loan Facility, a copy of which is attached hereto as Annex A.

"Loan Authorization Notice" shall mean the Loan Authorization Notice executed by Lender and delivered to Ex-Im Bank in accordance with the Delegated Authority Letter Agreement setting forth the terms and conditions of each Loan Facility.

"Loan Documents" shall mean the Loan Authorization Agreement, the Loan Agreement, this Agreement, each promissory note (if applicable), each Guarantee Agreement, and all other instruments, agreements and documents now or hereafter executed by the applicable Borrower, any Guarantor, Lender or Ex-Im Bank evidencing, securing, guaranteeing or otherwise relating to the Loan Facility or any Credit Accommodations made thereunder.

"Loan Facility" shall mean the Revolving Loan Facility, the Transaction Specific Loan Facility or the Transaction Specific Revolving Loan Facility established by Lender in favor of Borrower under the Loan Documents.

"Loan Facility Obligations" shall mean all loans, advances, debts, expenses, fees, liabilities, and obligations, including any accrued interest thereon, for the performance of covenants, tasks or duties or for payment of monetary amounts (whether or not such performance is then required or contingent, or amounts are liquidated or determinable) owing by Borrower to Lender, of any kind or nature, present or future, arising in connection with the Loan Facility.

"Loan Facility Term" shall mean, with respect to a Loan Facility, the number of months or portion thereof from the Effective Date to the Final Disbursement Date as set forth in the Loan Authorization Agreement as amended.

"Master Guarantee Agreement" shall mean the Master Guarantee Agreement between Ex-Im Bank and Lender, as amended, modified, supplemented and restated from time to time.

"Material Adverse Effect" shall mean a material adverse effect on (a) the business, assets, operations, prospects or financial or other condition of Borrower or any Guarantor, (b) any Borrower's ability to pay or perform the Loan Facility Obligations in accordance with the terms thereof, (c) the Collateral or Lender's Liens on the Collateral or the priority of such Lien, or (d) Lender's rights and remedies under the Loan Documents.

"Maximum Amount" shall mean the maximum Credit Accommodation Amount that may be outstanding at any time under each Loan Facility, as specified in Section 5.A. of the Loan Authorization Agreement.

"Other Assets" shall mean, with respect to a Loan Facility, such other assets of a Borrower to be included in Primary Collateral, which may include cash and marketable securities, or such other assets as Ex-Im Bank agrees to in writing, and disclosed as Primary Collateral in Section 6.A. of the Loan Authorization Agreement. The applicable Advance Rate (to be multiplied by the Other Asset Value) shall be as agreed to by Ex-Im Bank in writing case by case and set forth in Section 5.B.(4) of the Loan Authorization Agreement.

"Other Asset Value" shall mean, with respect to a Loan Facility, at the date of determination thereof, the value of the Other Assets as determined in accordance with GAAP.

"Other Collateral" shall mean any additional collateral that Lender customarily would require as security for loan facilities on its own account and risk where the permitted borrowing level is based principally on a borrowing base derived from a borrower's inventory and accounts receivable, but where such additional collateral does not enter into the borrowing base calculation.

"Permitted Liens" shall mean (a) Liens for taxes, assessments or other governmental charges or levies not delinquent, or, being contested in good faith and by appropriate proceedings and with respect to which proper reserves have been taken by Borrower; provided, that, the Lien shall have no effect on the priority of the Liens in favor of Lender or the value of the assets in which Lender has such a Lien and a stay of enforcement of any such Lien shall be in effect; (b) deposits or pledges securing obligations under worker's compensation, unemployment insurance, social security or public liability laws or similar legislation; (c) deposits or pledges securing bids, tenders, contracts (other than contracts for the payment of money), leases, statutory obligations, surety and appeal bonds and other obligations of like nature arising in the ordinary course of Borrower's business; (d) judgment Liens that have been stayed or bonded; (e) mechanics', workers', materialmen's or other like Liens arising in the ordinary course of Borrower's business with respect to obligations which are not due; (f) Liens placed upon fixed assets hereafter acquired to secure a portion of the purchase price thereof, provided, that, any such Lien shall not encumber any other property of Borrower; (g) security interests being terminated concurrently with the execution of the Loan Documents; and (h) Liens disclosed in Section 6.D. of the Loan

Authorization Agreement, provided that, except as otherwise permitted by Ex-Im Bank in writing, such Liens in Section 6.D. shall be subordinate to the Liens in favor of Lender on Primary Collateral.

"Person" shall mean any individual, sole proprietorship, partnership, limited liability partnership, joint venture, trust, unincorporated organization, association, corporation, limited liability company, institution, public benefit corporation, entity or government (whether national, federal, provincial, state, county, city, municipal or otherwise, including any instrumentality, division, agency, body or department thereof), and shall include such Person's successors and assigns.

"Pro Rata Percentage" shall mean, with respect to a Loan Facility, as of the date of determination thereof, the principal balance of the Credit Accommodations outstanding as a percentage of the combined principal balance of all loans from Lender to such Borrower including the then outstanding principal balance of the Credit Accommodations plus unfunded amounts under outstanding Letters of Credit.

"Principals" shall mean any officer, director, owner, partner, key employee, or other Person with primary management or supervisory responsibilities with respect to Borrower or any other Person (whether or not an employee) who has critical influence on or substantive control over the transactions covered by this Agreement.

"Retainage" shall mean that portion of the purchase price of an Export Order that a Buyer is not obligated to pay until the end of a specified period of time following the satisfactory performance under such Export Order.

"Retainage Accounts Receivable" shall mean those portions of Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable arising out of a Retainage.

"Retainage Value" shall mean, at the date of determination thereof, the aggregate face amount of Retainage Accounts Receivable as permitted by Ex-Im Bank in writing, less taxes, discounts, credits and allowances, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Revolving Loan Facility" shall mean the credit facility or portion thereof established by Lender in favor of Borrower for the purpose of providing working capital in the form of loans and/or Letters of Credit to finance the manufacture, production or purchase and subsequent export sale of Items pursuant to Loan Documents under which Credit Accommodations may be made and repaid on a continuous basis based solely on credit availability on the Export-Related Borrowing Base during the term of such credit facility

"Special Conditions" shall mean those conditions, if any, set forth in Section 13 of the Loan Authorization Agreement.

"Specific Export Orders" shall mean those Export Orders specified in Section 5.D. of the Loan Authorization Agreement as applicable for a Transaction Specific Revolving Loan Facility or a Transaction Specific Loan Facility.

"Standby Letters of Credit" shall mean those letters of credit subject to the ISP or UCP issued or caused to be issued by Lender for Borrower's account that can be drawn upon by a Buyer only if Borrower fails to perform all of its obligations with respect to an Export Order.

"Transaction Specific Loan Facility" shall mean a credit facility or a portion thereof established by Lender in favor of Borrower for the purpose of providing working capital in the form of loans and/or Letters of Credit to finance the manufacture, production or purchase and subsequent export sale of Items pursuant to Loan Documents under which Credit Accommodations are made based solely on credit availability on the Export-Related Borrowing Base relating to Specific Export Orders and once such Credit Accommodations are repaid they may not be reborrowed.

"Transaction Specific Revolving Loan Facility" shall mean a Revolving Credit Facility established to provide financing of Specific Export Orders.

"UCC" shall mean the Uniform Commercial Code, as the same may be in effect from time to time in the relevant United States jurisdiction.

"UCP" shall mean the Uniform Customs and Practice for Documentary Credits (1993 Revision), International Chamber of Commerce Publication No. 500 and any amendments and revisions thereof.

"U.S." or "United States" shall mean the United States of America including any division or agency thereof (including United States embassies or United States military bases located overseas), and any United States Territory (including without limitation, Puerto Rico, Guam or the United States Virgin Islands).

"U.S. Content" shall mean, with respect to any Item, all the costs, including labor, materials, services and overhead, but not markup or profit margin, which are of U.S. origin or manufacture, and which are incorporated into an Item in the United States.

"Warranty" shall mean Borrower's guarantee to Buyer that the Items will function as intended during the warranty period set forth in the applicable Export Order.

"Warranty Letter of Credit" shall mean a Standby Letter of Credit which is issued or caused to be issued by Lender to support the obligations of Borrower with respect to a Warranty or a Standby Letter of Credit which by its terms becomes a Warranty Letter of Credit.

1.02 Rules of Construction. For purposes of this Agreement, the following additional rules of construction shall apply, unless specifically indicated to the contrary: (a) wherever from the context it appears appropriate, each term stated in either the singular or plural shall include the singular and the plural, and pronouns stated in the masculine, feminine or neuter gender shall include the masculine, the feminine and the neuter; (b) the term "or" is not exclusive; (c) the term "including" (or any form thereof) shall not be limiting or exclusive; (d) all references to statutes and related regulations shall include any amendments of same and any successor statutes and regulations; (e) the words "this Agreement", "herein", "hereof", "hereunder" or other words of similar import refer to this Agreement as a whole including the schedules, exhibits, and annexes

hereto as the same may be amended, modified or supplemented; (f) all references in this Agreement to sections, schedules, exhibits, and annexes shall refer to the corresponding sections, schedules, exhibits, and annexes of or to this Agreement; and (g) all references to any instruments or agreements, including references to any of the Loan Documents, the Delegated Authority Letter Agreement, or the Fast Track Lender Agreement shall include any and all modifications, amendments and supplements thereto and any and all extensions or renewals thereof to the extent permitted under this Agreement.

1.03 Incorporation of Recitals. The Recitals to this Agreement are incorporated into and shall constitute a part of this Agreement.

ARTICLE II OBLIGATIONS OF BORROWER

Until payment in full of all Loan Facility Obligations and termination of the Loan Documents, Borrower agrees as follows:

2.01 Use of Credit Accommodations. (a) Borrower shall use Credit Accommodations only for the purpose of enabling Borrower to finance the cost of manufacturing, producing, purchasing or selling the Items. Borrower may not use any of the Credit Accommodations for the purpose of: (i) servicing or repaying any of Borrower's pre-existing or future indebtedness unrelated to the Loan Facility unless approved by Ex-Im Bank in writing; (ii) acquiring fixed assets or capital assets for use in Borrower's business; (iii) acquiring, equipping or renting commercial space outside of the United States; (iv) paying the salaries of non U.S. citizens or non-U.S. permanent residents who are located in offices outside of the United States; or (v) in connection with a Retainage or Warranty unless approved by Ex-Im Bank in writing.

(b) In addition, no Credit Accommodation may be used to finance the manufacture, purchase or sale of any of the following:

(i) Items to be sold to a Buyer located in a country as to which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;

(ii) that part of the cost of the Items which is not U.S. Content unless such part is not greater than fifty percent (50%) of the cost of the Items and is incorporated into the Items in the United States;

(iii) defense articles or defense services;

(iv) Capital Goods unless in accordance with Section 2.14 of this Agreement; or

(v) without Ex-Im Bank's prior written consent, any Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities.

2.02 Security Interests. Borrower agrees to cooperate with Lender in any steps Lender shall take to file and maintain valid, enforceable and perfected security interests in the Collateral.

2.03 Loan Documents and Loan Authorization Agreement. (a) This Agreement and each of the other Loan Documents applicable to Borrower have been duly executed and delivered on behalf of Borrower, and are and will continue to be legal and valid obligations of Borrower, enforceable against it in accordance with its terms.

(b) Borrower shall comply with all of the terms and conditions of this Agreement, the Loan Authorization Agreement and each of the other Loan Documents to which it is a party.

(c) Borrower hereby represents and warrants to Lender that Borrower is an Eligible Person.

2.04 Export-Related Borrowing Base Certificates and Export Orders. (a) In order to receive Credit Accommodations under the Loan Facility, Borrower shall have delivered to Lender an Export-Related Borrowing Base Certificate as frequently as required by Lender but at least within the past month, together with a copy of the Export Order(s) or, for Revolving Loan Facilities, if permitted by Lender, a written summary of the Export Orders (when Eligible Export-Related Inventory and Eligible Overseas Export-Related Inventory are entering the Export-Related Borrowing Base) against which Borrower is requesting Credit Accommodations. In addition, so long as there are any Credit Accommodations outstanding under the Loan Facility, Borrower shall deliver to Lender an Export-Related Borrowing Base Certificate at least once each month. Lender shall determine if daily electronic reporting reconciled monthly may substitute for monthly Export-Related Borrowing Base Certificates. If the Lender requires an Export-Related Borrowing Base Certificate more frequently, Borrower shall deliver such Export-Related Borrowing Base Certificate as required by Lender.

(b) If Lender permits summaries of Export Orders, Borrower shall also deliver promptly to Lender copies of any Export Orders requested by Lender.

2.05 Schedules, Reports and Other Statements. With the delivery of each Export-Related Borrowing Base Certificate required in Section 2.04 above, Borrower shall submit to Lender in writing (a) an Inventory schedule for the preceding month, as applicable, and (b) an Accounts Receivable Aging Report for the preceding month. Borrower shall also furnish to Lender promptly upon request such information, reports, contracts, invoices and other data concerning the Collateral as Lender may from time to time specify.

2.06 Exclusions from the Export-Related Borrowing Base. In determining the Export-Related Borrowing Base, Borrower shall exclude therefrom Inventory which are not Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory and Accounts Receivable which are not Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable. Borrower shall promptly, but in any event within five (5) Business Days, notify Lender (a) if any then existing Export-Related Inventory or Export-Related Overseas Inventory no longer constitutes Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory, as applicable or (b) of any event or circumstance which to Borrower's knowledge would cause Lender to consider any then existing Export-Related Accounts Receivable or Export-Related Overseas Accounts Receivable as no longer constituting an Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable, as applicable.

2.07 Borrowings and Reborrowings. (a) If the Loan Facility is a Revolving Loan Facility or Transaction Specific Revolving Loan Facility, provided that Borrower is not in default under any of the Loan Documents, Borrower may borrow, repay and reborrow amounts under such Loan Facility up to the credit available on the current Export-Related Borrowing Base Certificate subject to the terms of this Agreement and each of the other Loan Documents until the close of business on the Final Disbursement Date.

(b) If the Loan Facility is a Transaction Specific Loan Facility, provided that Borrower is not in default under any of the Loan Documents, Borrower may borrow (but not reborrow) amounts under the Loan Facility up to the credit available on the current Export-Related Borrowing Base Certificate subject to the terms of this Agreement and each of the other Loan Documents until the close of business on the Final Disbursement Date.

2.08 Repayment Terms. (a) The Borrower on a Revolving Loan Facility shall pay in full the outstanding Loan Facility Obligations no later than the first Business Day after the Final Disbursement Date unless such Loan Facility is renewed or extended by Lender consistent with procedures required by Ex-Im Bank.

(b) The Borrower on a Transaction Specific Loan Facility and a Transaction Specific Revolving Loan Facility shall, within two (2) Business Days of the receipt thereof, pay to Lender (for application against the outstanding Loan Facility Obligations) all checks, drafts, cash and other remittances it may receive in payment or on account of the Export-Related Accounts Receivable, Export-Related Overseas Accounts Receivable or any other Collateral, in precisely the form received (except for the endorsement of Borrower where necessary). Pending such deposit, Borrower shall hold such amounts in trust for Lender separate and apart and shall not commingle any such items of payment with any of its other funds or property. Unless a Transaction Specific Loan Facility or Transaction Specific Revolving Loan Facility is renewed or extended by Lender consistent with procedures required by Ex-Im Bank, Borrower shall pay in full all outstanding Loan Facility Obligations no later than the first Business Day after the Final Disbursement Date, except for Eligible Export-Related Accounts Receivables and Eligible Export-Related Overseas Accounts Receivable outstanding as of the Final Disbursement Date and due and payable after such date, for which the principal and accrued and unpaid interest thereon shall be due and payable no later than the first Business Day after the date such Accounts Receivable are due and payable.

2.09 Financial Statements. Borrower shall deliver to Lender the financial statements required to be delivered by Borrower in accordance with Section 11 of the Loan Authorization Agreement.

2.10 Additional Security or Payment. (a) Borrower shall at all times ensure that the Export-Related Borrowing Base equals or exceeds the aggregate outstanding amount of Disbursements. If informed by Lender or if Borrower otherwise has actual knowledge that the Export-Related Borrowing Base is at any time less than the aggregate outstanding amount of Disbursements, Borrower shall, within five (5) Business Days, either (i) furnish additional Collateral to Lender, in form and amount satisfactory to Lender and Ex-Im Bank or (ii) pay to Lender an amount equal to the difference between the aggregate outstanding amount of Disbursements and the Export-Related Borrowing Base.

(b) For purposes of this Agreement, in determining the Export-Related Borrowing Base there shall be deducted from the Export-Related Borrowing Base an amount equal to (i) twenty-five percent (25%) of the undrawn amount of outstanding Commercial Letters of Credit and Standby Letters of Credit and (ii) one hundred percent (100%) of the undrawn amount of outstanding Warranty Letters of Credit less the amount of cash collateral held by Lender to secure Warranty Letters of Credit.

(c) Unless otherwise approved in writing by Ex-Im Bank, for Revolving Loan Facilities (other than Transaction Specific Revolving Loan Facilities), Borrower shall at all times ensure that the sum of the outstanding amount of Disbursements and the undrawn amount of outstanding Commercial Letters of Credit that is supported by Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory (discounted by the relevant Advance Rate percentages) in the Export-Related Borrowing Base does not exceed sixty percent (60%) of the sum of the total outstanding amount of Disbursements and the undrawn amount of all outstanding Commercial Letters of Credit. If informed by Lender or if Borrower otherwise has actual knowledge that the sum of the outstanding amount of Disbursements and the undrawn amount of outstanding Commercial Letters of Credit that is supported by such Inventory exceeds sixty percent (60%) of the sum of the total outstanding Disbursements and the undrawn amount of all outstanding Commercial Letters of Credit, Borrower shall, within five (5) Business Days, either (i) furnish additional non-Inventory Collateral to Lender, in form and amount satisfactory to Lender and Ex-Im Bank, or (ii) pay down the applicable portion of the outstanding Disbursements or (iii) reduce the undrawn amount of outstanding Commercial Letters of Credit such that the above described ratio is not exceeded.

(d) If informed by Lender or if Borrower otherwise has actual knowledge that the conditions of Section 2.16(g) are at any time not being met, Borrower shall, within five (5) Business Days, either (i) furnish additional Collateral to Lender that is not Eligible Export-Related Overseas Accounts Receivable or Eligible Export-Related Overseas Inventory, in form and amount satisfactory to Lender and Ex-Im Bank, or (ii) remove from the Export-Related Borrowing Base the portion of Eligible Export-Related Overseas Accounts Receivable or Eligible Export-Related Overseas Inventory that supports greater than fifty percent (50%) of the Export-Related Borrowing Base.

2.11 Continued Security Interest. Borrower shall not change (a) its name or identity in any manner, (b) the location of its principal place of business or its jurisdiction of organization or formation, (c) the location of any of the Collateral or (d) the location of any of the books or records related to the Collateral, in each instance without giving thirty (30) days prior written notice thereof to Lender and taking all actions deemed necessary or appropriate by Lender to continuously protect and perfect Lender's Liens upon the Collateral.

2.12 Inspection of Collateral and Facilities. (a) Borrower shall permit the representatives of Lender and Ex-Im Bank to make at any time during normal business hours inspections of the Collateral and of Borrower's facilities, activities, and books and records, and shall cause its officers and employees to give full cooperation and assistance in connection therewith.

(b) Borrower agrees to facilitate Lender's conduct of field examinations at Borrower's facilities in accordance with the time schedule and content for such examinations

that Lender requests. Such field examinations shall address at a minimum: (x) the value of the Collateral against which Credit Accommodations may be provided, (y) the amount, if any, that the aggregate outstanding amount of Disbursements exceeds the Export-Related Borrowing Base and (z) whether such Borrower is in material compliance with the terms of each of the Loan Documents. Such field examinations shall include an inspection and evaluation of the Export-Related Inventory and Export-Related Overseas Inventory, a book audit of Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable, a review of the Accounts Receivable Aging Reports and a review of Borrower's compliance with any Special Conditions. Lenders who opt to use the Export-Related Historical Inventory Value in the Export-Related Borrowing Base calculation shall reconcile those numbers against the calculation for the relevant time periods using the Export-Related Inventory Value. Whenever Export-Related Accounts Receivable or Export-Related Inventory derived from Indirect Exports are in the Export-Related Borrowing Base, Lender shall verify compliance with Section 2.15 herein, including taking a random sampling of ultimate foreign purchasers.

2.13 General Intangibles. Borrower represents and warrants that it owns, or is licensed to use, all General Intangibles necessary to conduct its business as currently conducted except where the failure of Borrower to own or license such General Intangibles could not reasonably be expected to have a Material Adverse Effect.

2.14 Economic Impact Approval. (a) For Loan Facilities up to and including \$10 million, Borrower acknowledges that Capital Goods may not be included as Items, and Export-Related Inventory, Export-Related Overseas Inventory, Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable in connection with the sale of such Capital Goods may not be included in the Export-Related Borrowing Base, if such Capital Goods would enable a foreign buyer to establish or expand production of a product where, as of the date of the Economic Impact Certification covering such Item: (i) the Buyer is subject to a Final Anti-Dumping (AD) or Countervailing Duty (CVD) order, or a Suspension Agreement arising from a AD or CVD investigation, and such product is substantially the same as the product that is the subject of the AD/CVD order or suspension agreement; or (ii) the Buyer is the subject of a Section 201 injury determination by the International Trade Commission ("ITC") and such product is substantially the same as a product that is the subject of the ITC injury determination. Borrower may consult with Ex-Im Bank regarding the appropriate application of this Section 2.14(a) and may, at its option, request that Ex-Im Bank issue an Economic Impact Approval covering any Items listed in Section 4.A. of the Loan Authorization Agreement. For Loan Facilities over \$10 million involving Items that are Capital Goods, Borrower shall obtain from Ex-Im Bank, and abide by, an Economic Impact Approval covering all Items listed in Section 4(A) of the Loan Authorization Agreement.

(b) Borrower shall provide Lender with a certification in the form of Annex B (an "Economic Impact Certification") covering the Items stated in Section 4(A) of the Loan Authorization Agreement prior to Lender including such Items in the Loan Authorization Agreement. Prior to Lender amending the Loan Authorization Agreement to include additional Items, Borrower shall provide Lender with an additional Economic Impact Certification covering such additional Items.

2.15 Indirect Exports. Indirect Exports may be included as Items in a Loan Facility provided that funds available under such Loan Facility's Export-Related Borrowing Base

supported by Accounts Receivable and Inventory derived from Indirect Exports at no time exceed ten percent (10%) of the Maximum Amount of such Loan Facility, and provided, further that (a) the ultimate foreign buyer for the Items must be located in a country in which Ex-Im Bank is not legally prohibited from doing business in accordance with the Country Limitation Schedule, and (b) the Borrower must make available to Lender verifiable evidence of intent to export the Indirect Exports from the United States, which evidence may be contained in the Export Orders and Accounts Receivable Aging Reports and supporting documents. Lender must obtain written consent from Ex-Im Bank prior to including funds derived from Indirect Exports in an Export-Related Borrowing Base above the ten percent (10%) threshold.

2.16 Overseas Inventory and Accounts Receivable. Upon the prior written consent of Ex-Im Bank, Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory of a Borrower or of an Affiliated Foreign Person (as defined below) may be included in the Export-Related Borrowing Base provided that conditions required by Ex-Im Bank, including the following, are met:

- (a) the Affiliated Foreign Person, if any, has been approved by Ex-Im Bank;
- (b) the Affiliated Foreign Person, if any, is a Borrower under the relevant Loan Facility;
- (c) notwithstanding the Maximum Amount of the Loan Facility, all payments due and payable on such Export-Related Overseas Accounts Receivable are collected through a cash collateral account under Lender's control;
- (d) as of the Effective Date, or such later date when the Export-Related Overseas Accounts Receivable and/or Export-Related Overseas Inventory are added to the Loan Facility, Lender has obtained a valid and enforceable first priority Lien in the Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory, as applicable;
- (e) as of the Effective Date, or such later date when the Export-Related Overseas Accounts Receivable and/or Export-Related Overseas Inventory are added to the Loan Facility, Lender has obtained a legal opinion confirming the security interest in the Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory;
- (f) the Export-Related Overseas Accounts Receivable are due and payable in United States Dollars or other currency acceptable to Ex-Im Bank; and
- (g) at no time may the portion of the Export-Related Borrowing Base derived from Eligible Export-Related Overseas Accounts Receivable and Eligible Export-Related Overseas Inventory exceed fifty percent (50%) of the Export-Related Borrowing Base.

For purposes hereof, an "Affiliated Foreign Person" shall mean a subsidiary or affiliate of a Borrower on the same Loan Facility, which has duly executed as a Borrower all of the applicable Loan Documents and any other documents required by Ex-Im Bank, meets all of the requirements of the definition of Eligible Person other than subclause (a) thereof and is in good standing in the country of its formation or otherwise authorized to conduct business in such country.

2.17 Country Limitation Schedule. Unless otherwise informed in writing by Lender or Ex-Im Bank, Borrower shall be entitled to rely on the last copy of the Country Limitation Schedule distributed from Lender to Borrower.

2.18 Notice of Certain Events. Borrower shall promptly, but in any event within five (5) Business Days, notify Lender in writing of the occurrence of any of the following:

(a) Borrower or any Guarantor (i) applies for, consents to or suffers the appointment of, or the taking of possession by, a receiver, custodian, trustee, liquidator or similar fiduciary of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have dismissed within thirty (30) days, any petition filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;

(b) any Lien in any of the Collateral, granted or intended by the Loan Documents to be granted to Lender, ceases to be a valid, enforceable, perfected, first priority Lien (or a lesser priority if expressly permitted pursuant to Section 6 of the Loan Authorization Agreement) subject only to Permitted Liens;

(c) the issuance of any levy, assessment, attachment, seizure or Lien, other than a Permitted Lien, against any of the Collateral which is not stayed or lifted within thirty (30) calendar days;

(d) any proceeding is commenced by or against Borrower or any Guarantor for the liquidation of its assets or dissolution;

(e) any litigation is filed against Borrower or any Guarantor which has had or could reasonably be expected to have a Material Adverse Effect and such litigation is not withdrawn or dismissed within thirty (30) calendar days of the filing thereof;

(f) any default or event of default under the Loan Documents;

(g) any failure to comply with any terms of the Loan Authorization Agreement;

(h) any material provision of this Agreement or any other Loan Document for any reason ceases to be valid, binding and enforceable in accordance with its terms;

(i) any event which has had or could reasonably be expected to have a Material Adverse Effect; or

(j) the aggregate outstanding amount of Disbursements exceeds the applicable Export-Related Borrowing Base.

2.19 Insurance. Borrower will at all times carry property, liability and other insurance, with insurers acceptable to Lender, in such form and amounts, and with such deductibles and other provisions, as Lender shall require, and Borrower will provide evidence of such insurance to Lender on the proper Acord Form, so that Lender is satisfied that such insurance is, at all times, in full force and effect. Each property insurance policy shall name Lender as loss payee or mortgagee and shall contain a lender's loss payable endorsement in form acceptable to Lender and each liability insurance policy shall name Lender as an additional insured. All policies of insurance shall provide that they may not be cancelled or changed without at least thirty (30) days' prior written notice to Lender and shall otherwise be in form and substance satisfactory to Lender. Borrower will promptly deliver to Lender copies of all reports made to insurance companies.

2.20 Taxes. Borrower has timely filed all tax returns and reports required by applicable law, has timely paid all applicable taxes, assessments, deposits and contributions owing by Borrower and will timely pay all such items in the future as they become due and payable. Borrower may, however, defer payment of any contested taxes; provided, that Borrower (a) in good faith contests Borrower's obligation to pay such taxes by appropriate proceedings promptly and diligently instituted and conducted; (b) notifies Lender in writing of the commencement of, and any material development in, the proceedings; (c) posts bonds or takes any other steps required to keep the contested taxes from becoming a Lien upon any of the Collateral; and (d) maintains adequate reserves therefore in conformity with GAAP.

2.21 Compliance with Laws. Borrower represents and warrants that it has complied in all material respects with all provisions of all applicable laws and regulations, including those relating to Borrower's ownership of real or personal property, the conduct and licensing of Borrower's business, the payment and withholding of taxes, ERISA and other employee matters, safety and environmental matters.

2.22 Negative Covenants. Without the prior written consent of Ex-Im Bank and Lender, Borrower shall not: (a) merge, consolidate or otherwise combine with any other Person; (b) acquire all or substantially all of the assets or capital stock of any other Person; (c) sell, lease, transfer, convey, assign or otherwise dispose of any of its assets, except for the sale of Inventory in the ordinary course of business and the disposition of obsolete equipment in the ordinary course of business; (d) create any Lien on the Collateral except for Permitted Liens; (e) make any material changes in its organizational structure or identity; or (f) enter into any agreement to do any of the foregoing.

2.23 Cross Default. Borrower shall be deemed in default under the Loan Facility if Borrower fails to pay when due any amount payable to Lender under any loan or other credit accommodations to Borrower whether or not guaranteed by Ex-Im Bank.

2.24 Munitions List. If any of the Items are articles, services, or related technical data that are listed on the United States Munitions List (part 121 of title 22 of the Code of Federal Regulations), Borrower shall send a written notice promptly, but in any event within five (5) Business Days, of Borrower learning thereof to Lender describing the Items(s) and the corresponding invoice amount

2.25 Suspension and Debarment, etc. On the date of this Agreement neither Borrower nor its Principals are (a) debarred, suspended, proposed for debarment with a final determination

still pending, declared ineligible or voluntarily excluded (as such terms are defined under any of the Debarment Regulations referred to below) from participating in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations or (b) indicted, convicted or had a civil judgment rendered against Borrower or any of its Principals for any of the offenses listed in any of the Debarment Regulations. Unless authorized by Ex-Im Bank, Borrower will not knowingly enter into any transactions in connection with the Items with any person who is debarred, suspended, declared ineligible or voluntarily excluded from participation in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations. Borrower will provide immediate written notice to Lender if at any time it learns that the certification set forth in this Section 2.24 was erroneous when made or has become erroneous by reason of changed circumstances.

ARTICLE III RIGHTS AND REMEDIES

3.01 Indemnification. Upon Ex-Im Bank's payment of a Claim to Lender in connection with the Loan Facility pursuant to the Master Guarantee Agreement, Ex-Im Bank may assume all rights and remedies of Lender under the Loan Documents and may enforce any such rights or remedies against Borrower, the Collateral and any Guarantors. Borrower shall hold Ex-Im Bank and Lender harmless from and indemnify them against any and all liabilities, damages, claims, costs and losses incurred or suffered by either of them resulting from (a) any materially incorrect certification or statement knowingly made by Borrower or its agent to Ex-Im Bank or Lender in connection with the Loan Facility, this Agreement, the Loan Authorization Agreement or any other Loan Documents or (b) any material breach by Borrower of the terms and conditions of this Agreement, the Loan Authorization Agreement or any of the other Loan Documents. Borrower also acknowledges that any statement, certification or representation made by Borrower in connection with the Loan Facility is subject to the penalties provided in Article 18 U.S.C. Section 1001.

3.02 Liens. Borrower agrees that any and all Liens granted by it to Lender are also hereby granted to Ex-Im Bank to secure Borrower's obligation, however arising, to reimburse Ex-Im Bank for any payments made by Ex-Im Bank pursuant to the Master Guarantee Agreement. Lender is authorized to apply the proceeds of, and recoveries from, any property subject to such Liens to the satisfaction of Loan Facility Obligations in accordance with the terms of any agreement between Lender and Ex-Im Bank.

**ARTICLE IV
MISCELLANEOUS**

4.01 Governing Law. This Agreement and the obligations arising under this Agreement shall be governed by, and construed in accordance with, the law of the state governing the Loan Agreement.

4.02 Notification. All notices required by this Agreement shall be given in the manner and to the parties provided for in the Loan Agreement.

4.03 Partial Invalidity. If at any time any of the provisions of this Agreement becomes illegal, invalid or unenforceable in any respect under the law of any jurisdiction, neither the legality, the validity nor the enforceability of the remaining provisions hereof shall in any way be affected or impaired.

4.04 Waiver of Jury Trial. BORROWER HEREBY KNOWINGLY, VOLUNTARILY AND INTENTIONALLY WAIVES ANY AND ALL RIGHTS IT MAY HAVE TO A TRIAL BY JURY IN RESPECT OF ANY ACTION, SUIT, PROCEEDING OR OTHER LITIGATION BROUGHT TO RESOLVE ANY DISPUTE ARISING UNDER, ARISING OUT OF OR IN CONNECTION WITH THIS AGREEMENT, THE LOAN AUTHORIZATION AGREEMENT, ANY LOAN DOCUMENT, OR ANY OTHER AGREEMENT, DOCUMENT OR INSTRUMENT EXECUTED OR DELIVERED IN CONNECTION HEREWITH OR THEREWITH OR ANY COURSE OF CONDUCT, COURSE OF DEALING, STATEMENTS (WHETHER VERBAL OR WRITTEN), OR ACTIONS OR OMISSIONS OF LENDER, EX-IM BANK, OR ANY OTHER PERSON, RELATING TO THIS AGREEMENT, THE LOAN AUTHORIZATION AGREEMENT OR ANY OTHER LOAN DOCUMENT.

4.05 Consequential Damages. Neither Ex-Im Bank, Lender nor any agent or attorney for any of them shall be liable to Borrower for consequential damages arising from any breach of contract, tort or other wrong relating to the establishment, administration or collection of the Loan Facility Obligations.

IN WITNESS WHEREOF, Borrower has caused this Agreement to be duly executed as the 6th day of March, 2018.

BIOLASE, INC.
(Name of Borrower)

By: /s/ John R. Beaver
(Signature)

Name: John R. Beaver
(Print or Type)

Title: SVP and Chief Financial Officer
(Print or Type)

ACKNOWLEDGED:
WESTERN ALLIANCE BANK
(Name of Lender)

By: /s/ Brenda Penrod
(Signature)

Name: Brenda Penrod
(Print or Type)

Title: Vice President
(Print or Type)

ANNEXES:

- Annex A - Loan Authorization Agreement, Fast Track Loan Authorization Agreement or Loan Authorization Notice, as applicable
- Annex B - Economic Impact Certification

CONSENT OF GUARANTORS

Each of the undersigned as a Guarantor of the obligations of Borrower to the Lender executing the foregoing Agreement hereby agrees that the foregoing Agreement, each of their respective Guarantee Agreements and each other Loan Documents may be assigned to the Export-Import Bank of the United States.

[INDIVIDUAL GUARANTOR]

[CORPORATE GUARANTOR]

B y : _____

N a m e : _____

Title:

**EXPORT-IMPORT BANK OF THE UNITED STATES
WORKING CAPITAL GUARANTEE PROGRAM**

BORROWER AGREEMENT

Ex-Im Bank 12/31/05

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**EXPORT-IMPORT BANK OF THE UNITED STATES WORKING
CAPITAL GUARANTEE PROGRAM BORROWER
AGREEMENT**

THIS BORROWER AGREEMENT (this "Agreement") is made and entered into by the entity identified as Borrower on the signature page hereof ("Borrower") in favor of the Export-Import Bank of the United States ("Ex-Im Bank") and the institution identified as Lender on the signature page hereof ("Lender").

RECITALS

Borrower has requested that Lender establish a Loan Facility in favor of Borrower for the purposes of providing Borrower with working capital to finance the manufacture, production or purchase and subsequent export sale of Items.

Lender and Borrower expect that Ex-Im Bank will provide a guarantee to Lender regarding this Loan Facility subject to the terms and conditions of the Master Guarantee Agreement, a Loan Authorization Agreement, and to the extent applicable, the Delegated Authority Letter Agreement or Fast Track Lender Agreement.

Lender and Ex-Im Bank have requested that Borrower execute this Agreement as a condition precedent to Lender establishing the Loan Facility and Ex-Im Bank providing the guarantee.

NOW, THEREFORE, Borrower hereby agrees as follows:

**ARTICLE I
DEFINITIONS**

1.01 Definition of Terms. As used in this Agreement, including the Recitals to this Agreement and the Loan Authorization Agreement, the following terms shall have the following meanings:

"Accounts Receivable" shall mean all of Borrower's now owned or hereafter acquired (a) "accounts" (as such term is defined in the UCC), other receivables, book debts and other forms of obligations, whether arising out of goods sold or services rendered or from any other transaction; (b) rights in, to and under all purchase orders or receipts for goods or services; (c) rights to any goods represented or purported to be represented by any of the foregoing (including unpaid sellers' rights of rescission, replevin, reclamation and stoppage in transit and rights to returned, reclaimed or repossessed goods); (d) moneys due or to become due to such Borrower under all purchase orders and contracts (which includes Export Orders) for the sale of goods or the performance of services or both by Borrower (whether or not yet earned by performance on the part of Borrower), including the proceeds of the foregoing; (e) any notes, drafts, letters of credit, insurance proceeds or other instruments, documents and writings evidencing or supporting the foregoing; and (f) all collateral security and guarantees of any kind given by any other Person with respect to any of the foregoing.

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“Accounts Receivable Aging Report” shall mean a report detailing the Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable for a Loan Facility, and the applicable terms for the relevant time period; in the case of Indirect Exports, such report shall indicate the portion of such Accounts Receivables corresponding to Indirect Exports.

"Advance Rate" shall mean, with respect to a Loan Facility, the rate specified in Section 5.C. of the Loan Authorization Agreement for each category of Primary Collateral except for Export-Related General Intangibles and Other Collateral. Unless otherwise set forth in writing by Ex-Im Bank, in no event shall the Advance Rate exceed (i) ninety percent (90%) for Eligible Export-Related Accounts Receivable, (ii) seventy five percent (75%) for Eligible Export-Related Inventory, (iii) seventy percent (70%) for Eligible Export-Related Overseas Accounts Receivable or (iv) sixty percent (60%) for Eligible Export-Related Overseas Inventory and (v) twenty five percent (25%) for Retainage Accounts Receivable.

“Affiliated Foreign Person” shall have the meaning set forth in Section 2.15.

"Business Day" shall mean any day on which the Federal Reserve Bank of New York is open for business.

"Buyer" shall mean a Person that has entered into one or more Export Orders with Borrower or who is an obligor on Export-Related Accounts Receivable or Export-Related Overseas Accounts Receivable.

“Capital Good” shall mean a capital good (e.g., manufacturing equipment, licensing agreements) that will establish or expand foreign production capacity of an exportable good.

"Collateral" shall mean all real and personal property and interest in real and personal property in or upon which Lender has been, or shall be, granted a Lien as security for the payment of all the Loan Facility Obligations and all products and proceeds (cash and non-cash) thereof.

"Commercial Letters of Credit" shall mean those letters of credit subject to the UCP payable in Dollars and issued or caused to be issued by Lender on behalf of Borrower under a Loan Facility for the benefit of a supplier(s) of Borrower in connection with Borrower's purchase of goods or services from the supplier in support of the export of the Items.

"Country Limitation Schedule" shall mean the schedule published from time to time by Ex-Im Bank setting forth on a country by country basis whether and under what conditions ExIm Bank will provide coverage for the financing of export transactions to countries listed therein.

“Credit Accommodation Amount” shall mean, the sum of (a) the aggregate outstanding amount of Disbursements and (b) the aggregate outstanding Letter of Credit Obligations, which sum may not exceed the Maximum Amount.

"Credit Accommodations" shall mean, collectively, Disbursements and Letter of Credit Obligations.

"Debarment Regulations" shall mean, collectively, (a) the Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 53 Fed. Reg. 19204 (May 26, 1988), (b) Subpart 9.4 (Debarment, Suspension, and Ineligibility) of the Federal Acquisition Regulations, 48 C.F.R. 9.400-9.409 and (c) the revised Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 60 Fed. Reg. 33037 (June 26, 1995).

"Delegated Authority Letter Agreement" shall mean the Delegated Authority Letter Agreement, if any, between Ex-Im Bank and Lender.

"Disbursement" shall mean, collectively, (a) an advance of a working capital loan from Lender to Borrower under the Loan Facility, and (b) an advance to fund a drawing under a Letter of Credit issued or caused to be issued by Lender for the account of Borrower under the Loan Facility.

"Dollars" or "\$" shall mean the lawful currency of the United States.

"Economic Impact Approval" shall mean a written approval issued by Ex-Im Bank stating the conditions under which a Capital Good may be included as an Item in a Loan Facility consistent with Ex-Im Bank's economic impact procedures (or other mechanism for making this determination that Ex-Im Bank notifies Lender of in writing).

"Economic Impact Certification" shall have the meaning set forth in Section 2.14(b).

"Effective Date" shall mean the date on which (a) all of the Loan Documents have been executed by Lender, Borrower and, if applicable, Ex-Im Bank and (b) all of the conditions to the making of the initial Credit Accommodations under the Loan Documents or any amendments thereto have been satisfied.

"Eligible Export-Related Accounts Receivable" shall mean Export-Related Accounts Receivable which are acceptable to Lender and which are deemed to be eligible pursuant to the Loan Documents, but in no event shall Eligible Export-Related Accounts Receivable include any Account Receivable:

- (a) that does not arise from the sale of Items in the ordinary course of Borrower's business;
- (b) that is not subject to a valid, perfected first priority Lien in favor of Lender;
- (c) as to which any covenant, representation or warranty contained in the Loan Documents with respect to such Account Receivable has been breached;
- (d) that is not owned by Borrower or is subject to any right, claim or interest of another Person other than the Lien in favor of Lender;
- (e) with respect to which an invoice has not been sent;
- (f) that arises from the sale of defense articles or defense services;

- (g) that arises from the sale of Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities unless with Ex-Im Bank's prior written consent;
- (h) that is due and payable from a Buyer located in a country with which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;
- (i) that does not comply with the requirements of the Country Limitation Schedule;
- (j) that is due and payable more than one hundred eighty (180) days from the date of the invoice;
- (k) that is not paid within sixty (60) calendar days from its original due date, unless it is insured through Ex-Im Bank export credit insurance for comprehensive commercial and political risk, or through Ex-Im Bank approved private insurers for comparable coverage, in which case it is not paid within ninety (90) calendar days from its due date;
- (l) of a Buyer for whom fifty percent (50%) or more of the Accounts Receivable of such Buyer do not satisfy the requirements of subclauses (j) and (k) above;
- (m) that arises from a sale of goods to or performance of services for an employee of Borrower, a stockholder of Borrower, a subsidiary of Borrower, a Person with a controlling interest in Borrower or a Person which shares common controlling ownership with Borrower;
- (n) that is backed by a letter of credit unless the Items covered by the subject letter of credit have been shipped;
- (o) that Lender or Ex-Im Bank, in its reasonable judgment, deems uncollectible for any reason;
- (p) that is due and payable in a currency other than Dollars, except as may be approved in writing by Ex-Im Bank;
- (q) that is due and payable from a military Buyer, except as may be approved in writing by Ex-Im Bank;
- (r) that does not comply with the terms of sale set forth in Section 7 of the Loan Authorization Agreement;
- (s) that is due and payable from a Buyer who (i) applies for, suffers, or consents to the appointment of, or the taking of possession by, a receiver, custodian, trustee or liquidator of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have

dismissed, any petition which is filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;

(t) that arises from a bill-and-hold, guaranteed sale, sale-and-return, sale on approval, consignment or any other repurchase or return basis or is evidenced by chattel paper;

(u) for which the Items giving rise to such Accounts Receivable have not been shipped to the Buyer or when the Items are services, such services have not been performed or when the Export Order specifies a timing for invoicing the Items other than shipment or performance and the Items have not been invoiced in accordance with such terms of the Export Order, or the Accounts Receivable otherwise do not represent a final sale;

(v) that is subject to any offset, deduction, defense, dispute, or counterclaim or the Buyer is also a creditor or supplier of Borrower or the Account Receivable is contingent in any respect or for any reason;

(w) for which Borrower has made any agreement with the Buyer for any deduction therefrom, except for discounts or allowances made in the ordinary course of business for prompt payment, all of which discounts or allowances are reflected in the calculation of the face value of each respective invoice related thereto;

(x) for which any of the Items giving rise to such Account Receivable have been returned, rejected or repossessed;

(y) that is included as an eligible receivable under any other credit facility to which Borrower is a party;

(z) any of the Items giving rise to such Accounts Receivable are Capital Goods, unless the transaction is in accordance with Section 2.14;

(aa) that is due and payable from a Buyer that is, or is located in, the United States; provided however, that this subsection (aa) shall not preclude an Export-Related Accounts Receivable arising from the sale of Items to foreign contractors or subcontractors providing services to a United States Embassy or the United States Military located overseas from being deemed an Eligible Export-Related Accounts Receivable; or

(bb) that arises from the sale of Items that do not meet the U.S. Content requirements in accordance with Section 2.01(b) (ii).

"Eligible Export-Related Inventory" shall mean Export-Related Inventory which is acceptable to Lender and which is deemed to be eligible pursuant to the Loan Documents, but in no event shall Eligible Export-Related Inventory include any Inventory:

(a) that is not subject to a valid, perfected first priority Lien in favor of Lender;

(b) that is located at an address that has not been disclosed to Lender in writing;

- (c) that is placed by Borrower on consignment or held by Borrower on consignment from another Person;
- (d) that is in the possession of a processor or bailee, or located on premises leased or subleased to Borrower, or on premises subject to a mortgage in favor of a Person other than Lender, unless such processor or bailee or mortgagee or the lessor or sublessor of such premises, as the case may be, has executed and delivered all documentation which Lender shall require to evidence the subordination or other limitation or extinguishment of such Person's rights with respect to such Inventory and Lender's right to gain access thereto;
- (e) that is produced in violation of the Fair Labor Standards Act or subject to the "hot goods" provisions contained in 29 U.S.C. §215 or any successor statute or section;
- (f) as to which any covenant, representation or warranty with respect to such Inventory contained in the Loan Documents has been breached;
- (g) that is not located in the United States unless expressly permitted by Lender, on terms acceptable to Lender;
- (h) that is an Item or is to be incorporated into Items that do not meet U.S. Content requirements in accordance with Section 2.01(b)(ii);
- (i) that is demonstration Inventory;
- (j) that consists of proprietary software (i.e. software designed solely for Borrower's internal use and not intended for resale);
- (k) that is damaged, obsolete, returned, defective, recalled or unfit for further processing;
- (l) that has been previously exported from the United States;
- (m) that constitutes, or will be incorporated into Items that constitute, defense articles or defense services;
- (n) that is an Item or will be incorporated into Items that will be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities unless with Ex-Im Bank's prior written consent;
- (o) that is an Item or is to be incorporated into Items destined for shipment to a country as to which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;
- (p) that is an Item or is to be incorporated into Items destined for shipment to a Buyer located in a country in which Ex-Im Bank coverage is not available for commercial reasons as designated in the Country Limitation Schedule, unless and only to the extent that such Items are to be sold to such country on terms of a letter of credit confirmed by a bank acceptable to Ex-Im Bank;

(q) that constitutes, or is to be incorporated into, Items whose sale would result in an Accounts Receivable which would not be an Eligible Export-Related Accounts Receivable;

(r) that is included as eligible inventory under any other credit facility to which Borrower is a party; or

(s) that is, or is to be incorporated into, an Item that is a Capital Good, unless the transaction is in accordance with Section 2.14.

"Eligible Export-Related Overseas Accounts Receivable" shall mean Export-Related Overseas Accounts Receivable which are acceptable to Lender and which are deemed to be eligible pursuant to the Loan Documents but in no event shall include the Accounts Receivable (a) through (bb) excluded from the definition of Eligible Export-Related Accounts Receivable.

"Eligible Export-Related Overseas Inventory" shall mean Export-Related Overseas Inventory which is acceptable to Lender and which is deemed to be eligible pursuant to the Loan Documents, but in no event shall include the Inventory (a) through (r) excluded from the definition of Eligible Export-Related Inventory.

"Eligible Person" shall mean a sole proprietorship, partnership, limited liability partnership, corporation or limited liability company which (a) is domiciled, organized or formed, as the case may be, in the United States, whether or not such entity is owned by a foreign national or foreign entity; (b) is in good standing in the state of its formation or otherwise authorized to conduct business in the United States; (c) is not currently suspended or debarred from doing business with the United States government or any instrumentality, division, agency or department thereof; (d) exports or plans to export Items; (e) operates and has operated as a going concern for at least one (1) year; (f) has a positive tangible net worth determined in accordance with GAAP; and (g) has revenue generating operations relating to its core business activities for at least one year. An Affiliated Foreign Person that meets all of the requirements of the foregoing definition of Eligible Person other than subclause (a) thereof shall be deemed to be an Eligible Person

"ERISA" shall mean the Employee Retirement Income Security Act of 1974 and the rules and regulations promulgated thereunder

"Export Order" shall mean a documented purchase order or contract evidencing a Buyer's agreement to purchase the Items from Borrower for export from the United States, which documentation shall include written information that is necessary to confirm such purchase order or contract, including identification of the Items, the name of the Buyer, the country of destination, contact information for the Buyer and the total amount of the purchase order or contract; in the case of Indirect Exports, such documentation shall further include a copy of the written purchase order or contract from a foreign purchaser or other documentation clearly evidencing a foreign purchaser's agreement to purchase the Items.

"Export-Related Accounts Receivable" shall mean those Accounts Receivable arising from the sale of Items which are due and payable to Borrower in the United States.

"Export-Related Accounts Receivable Value" shall mean, at the date of determination thereof, the aggregate face amount of Eligible Export-Related Accounts Receivable less taxes, discounts, credits, allowances and Retainages, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Export-Related Borrowing Base" shall mean, at the date of determination thereof, the sum of (a) (if Lender elects to include) the Export-Related Inventory Value or Export-Related Historical Inventory Value multiplied by the Advance Rate applicable to Eligible Export-Related Inventory set forth in Section 5.B.(1.) of the Loan Authorization Agreement, plus (b) the Export-Related Accounts Receivable Value multiplied by the Advance Rate applicable to Eligible Export-Related Accounts Receivable set forth in Section 5.B.(2.) of the Loan Authorization Agreement, plus (c) if permitted by Ex-Im Bank in writing, the Retainage Value multiplied by the Advance Rate applicable to Retainages set forth in Section 5.B.(3.) of the Loan Authorization Agreement, plus (d) the Other Assets set forth in Section 5.B.(4.) of the Loan Authorization Agreement multiplied by the Advance Rate agreed to in writing by Ex-Im Bank, plus (e) if permitted by Ex-Im Bank in writing, the Export-Related Overseas Accounts Receivable Value multiplied by the Advance Rate applicable to Eligible Export-Related Overseas Accounts Receivable set forth in Section 5.B.(5.) of the Loan Authorization Agreement, plus (f) if permitted by Ex-Im Bank in writing, the Export-Related Overseas Inventory Value multiplied by the Advance Rate applicable to Eligible Export-Related Overseas Inventory set forth in Section 5.B.(6.) of the Loan Authorization Agreement, less (g) the amounts required to be reserved pursuant to Sections 4.12 and 4.13 of this Agreement for each outstanding Letter of Credit, less (h) such reserves and in such amounts deemed necessary and proper by Lender from time to time.

"Export-Related Borrowing Base Certificate" shall mean a certificate in the form provided or approved by Lender, executed by Borrower and delivered to Lender pursuant to the Loan Documents detailing the Export-Related Borrowing Base supporting the Credit Accommodations which reflects, to the extent included in the Export-Related Borrowing Base, Export-Related Accounts Receivable, Eligible Export-Related Accounts Receivable, Export-Related Inventory, Eligible Export-Related Inventory, Export-Related Overseas Accounts Receivable, Eligible Export-Related Accounts Receivable, Export-Related Overseas Inventory and Eligible Export-Related Overseas Inventory balances that have been reconciled with Borrower's general ledger, Accounts Receivable Aging Report and Inventory schedule.

"Export-Related General Intangibles" shall mean the Pro Rata Percentage of General Intangibles determined as of the earlier of: (i) the date such General Intangibles are liquidated and (ii) the date Borrower fails to pay when due any outstanding amount of principal or accrued interest payable under the Loan Documents that becomes the basis for a Payment Default on which a Claim is filed.

"Export-Related Historical Inventory Value" shall mean with respect to a Borrower, the relevant Export-Related Sales Ratio multiplied by the lowest of (i) the cost of such Borrower's Inventory as determined in accordance with GAAP, or (ii) the market value of such Borrower's Inventory as determined in accordance with GAAP or (iii) the appraised or orderly liquidation value of such Borrower's Inventory, if Lender has loans and financial accommodations to such Borrower for which it conducts (or contracts for the performance of) such an appraised or orderly liquidation value.

"Export-Related Inventory" shall mean the Inventory of Borrower located in the United States that has been purchased, manufactured or otherwise acquired by Borrower for sale or resale as Items, or to be incorporated into Items to be sold or resold pursuant to Export Orders.

"Export-Related Inventory Value" shall mean, at the date of determination thereof, the lowest of (i) the cost of Eligible Exported-Related Inventory as determined in accordance with GAAP, or (ii) the market value of Eligible Export-Related Inventory as determined in accordance with GAAP or (iii) the lower of the appraised market value or orderly liquidation value of the Eligible Export-Related Inventory, if Lender has other loans and financial accommodations to a Borrower for which it conducts (or contracts for the performance of) such an appraised or orderly liquidation value.

"Export-Related Overseas Accounts Receivable" shall mean those Accounts Receivable arising from the sale of Items which are due and payable outside of the United States either to a Borrower or an Affiliated Foreign Person.

"Export-Related Overseas Accounts Receivable Value" shall mean, with respect to a Loan Facility, at the date of determination thereof, the aggregate face amount of Eligible Export-Related Overseas Accounts Receivable less taxes, discounts, credits, allowances and Retainages, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Export-Related Overseas Inventory" shall mean the Inventory of Borrower located outside of the United States that has been purchased, manufactured or otherwise acquired by such Borrower for sale or resale as Items, or to be incorporated into Items to be sold or resold pursuant to Export Orders.

"Export-Related Overseas Inventory Value" shall mean, at the date of determination thereof, the lowest of (i) the cost of Eligible Export-Related Overseas Inventory as determined in accordance with GAAP, (ii) the market value of Eligible Export-Related Overseas Inventory as determined in accordance with GAAP or (iii) the appraised or orderly liquidation value of the Eligible Export-Related Overseas Inventory, if Lender has other loans and financial accommodations to Borrower or an Affiliated Foreign Person for which it conducts (or contracts for the performance of) such a appraised or orderly liquidation.

"Export-Related Sales Ratio" shall mean with respect to a Borrower, the percentage of such Borrower's total sales revenue derived from the sale of Eligible Export-Related Inventory over a rolling twelve-month period ending no more than ninety (90) days prior to the date of the relevant Export-Related Borrowing Base Certificate

"Extension" shall mean, with respect to a Loan Facility, an amendment to the Loan Authorization Agreement extending the Final Disbursement Date on the same terms and conditions as the Loan Facility for an aggregate period not to exceed one hundred and twenty (120) days beyond the original Final Disbursement Date, either as agreed to in writing by Ex-Im Bank or, in the case of Delegated Authority, as notified by Lender to Ex-Im Bank pursuant to its authority under the Delegated Authority Letter Agreement.

"Fast Track Lender Agreement" shall mean the Fast Track Lender Agreement, if any, between Ex-Im Bank and Lender.

"Final Disbursement Date" shall mean the last date on which Lender may make a Disbursement set forth in Section 10 of the Loan Authorization Agreement (including as amended by an Extension) or, if such date is not a Business Day, the next succeeding Business Day; provided, however, to the extent that Lender has not received cash collateral in the amount of the Letter of Credit Obligations or an equivalent full indemnity from Borrower or Guarantor, as applicable, with respect to Letter of Credit Obligations outstanding on the Final Disbursement Date, the Final Disbursement Date with respect to an advance to fund a drawing under such Letter of Credit shall be no later than thirty (30) days after any such drawing which may be no later than the expiry date of the Letter of Credit related thereto.

"GAAP" shall mean the generally accepted accounting principles issued in the United States.

"General Intangibles" shall mean all intellectual property and other "general intangibles" (as such term is defined in the UCC).

"Guarantor" shall mean any Person which is identified in Section 3 of the Loan Authorization Agreement who shall guarantee (jointly and severally if more than one) the payment and performance of all or a portion of the Loan Facility Obligations.

"Guarantee Agreement" shall mean a valid and enforceable agreement of guarantee executed by each Guarantor in favor of Lender.

"Indirect Exports" shall mean finished goods or services that are sold by a Borrower to a Buyer located in the United States, are intended for export from the United States, and are identified in Section 4.A.(2.) of the Loan Authorization Agreement.

"Inventory" shall mean all "inventory" (as such term is defined in the UCC), now or hereafter owned or acquired by Borrower, wherever located, including all inventory, merchandise, goods and other personal property which are held by or on behalf of Borrower for sale or lease or are furnished or are to be furnished under a contract of service or which constitute raw materials, work in process or materials used or consumed or to be used or consumed in Borrower's business or in the processing, production, packaging, promotion, delivery or shipping of the same, including other supplies.

"ISP" shall mean the International Standby Practices-ISP98, International Chamber of Commerce Publication No. 590 and any amendments and revisions thereof.

"Issuing Bank" shall mean the bank that issues a Letter of Credit, which bank is Lender itself or a bank that Lender has caused to issue a Letter of Credit by way of a guarantee or reimbursement obligation.

"Items" shall mean the finished goods or services which are intended for export from the United States, either directly or as an Indirect Export, meet the U.S. Content requirements in

accordance with Section 2.01(b)(ii) of this Agreement and are specified in Section 4.A. of the Loan Authorization Agreement.

"Letter of Credit" shall mean a Commercial Letter of Credit or a Standby Letter of Credit.

"Letter of Credit Obligations" shall mean all undrawn amounts of outstanding obligations incurred by Lender, whether direct or indirect, contingent or otherwise, due or not due, in connection with the issuance or guarantee by Lender or Issuing Bank of Letters of Credit.

"Lien" shall mean any mortgage, security deed or deed of trust, pledge, hypothecation, assignment, deposit arrangement, lien, charge, claim, security interest, security title, easement or encumbrance, or preference, priority or other security agreement or preferential arrangement of any kind or nature whatsoever (including any lease or title retention agreement, any financing lease having substantially the same economic effect as any of the foregoing, and the filing of, or agreement to give, any financing statement perfecting a security interest under the UCC or comparable law of any jurisdiction) by which property is encumbered or otherwise charged.

"Loan Agreement" shall mean a valid and enforceable agreement between Lender and a Borrower setting forth, with respect to each Loan Facility, the terms and conditions of such Loan Facility.

"Loan Authorization Agreement" shall mean, as applicable, the duly executed Loan Authorization Agreement, Fast Track Loan Authorization Agreement, or the Loan Authorization Notice, setting forth certain terms and conditions of each Loan Facility, a copy of which is attached hereto as Annex A.

"Loan Authorization Notice" shall mean the Loan Authorization Notice executed by Lender and delivered to Ex-Im Bank in accordance with the Delegated Authority Letter Agreement setting forth the terms and conditions of each Loan Facility.

"Loan Documents" shall mean the Loan Authorization Agreement, the Loan Agreement, this Agreement, each promissory note (if applicable), each Guarantee Agreement, and all other instruments, agreements and documents now or hereafter executed by the applicable Borrower, any Guarantor, Lender or Ex-Im Bank evidencing, securing, guaranteeing or otherwise relating to the Loan Facility or any Credit Accommodations made thereunder.

"Loan Facility" shall mean the Revolving Loan Facility, the Transaction Specific Loan Facility or the Transaction Specific Revolving Loan Facility established by Lender in favor of Borrower under the Loan Documents.

"Loan Facility Obligations" shall mean all loans, advances, debts, expenses, fees, liabilities, and obligations, including any accrued interest thereon, for the performance of covenants, tasks or duties or for payment of monetary amounts (whether or not such performance is then required or contingent, or amounts are liquidated or determinable) owing by Borrower to Lender, of any kind or nature, present or future, arising in connection with the Loan Facility.

"Loan Facility Term" shall mean, with respect to a Loan Facility, the number of months or portion thereof from the Effective Date to the Final Disbursement Date as set forth in the Loan Authorization Agreement as amended.

"Master Guarantee Agreement" shall mean the Master Guarantee Agreement between Ex-Im Bank and Lender, as amended, modified, supplemented and restated from time to time.

"Material Adverse Effect" shall mean a material adverse effect on (a) the business, assets, operations, prospects or financial or other condition of Borrower or any Guarantor, (b) any Borrower's ability to pay or perform the Loan Facility Obligations in accordance with the terms thereof, (c) the Collateral or Lender's Liens on the Collateral or the priority of such Lien, or (d) Lender's rights and remedies under the Loan Documents.

"Maximum Amount" shall mean the maximum Credit Accommodation Amount that may be outstanding at any time under each Loan Facility, as specified in Section 5.A. of the Loan Authorization Agreement.

"Other Assets" shall mean, with respect to a Loan Facility, such other assets of a Borrower to be included in Primary Collateral, which may include cash and marketable securities, or such other assets as Ex-Im Bank agrees to in writing, and disclosed as Primary Collateral in Section 6.A. of the Loan Authorization Agreement. The applicable Advance Rate (to be multiplied by the Other Asset Value) shall be as agreed to by Ex-Im Bank in writing case by case and set forth in Section 5.B.(4) of the Loan Authorization Agreement.

"Other Asset Value" shall mean, with respect to a Loan Facility, at the date of determination thereof, the value of the Other Assets as determined in accordance with GAAP.

"Other Collateral" shall mean any additional collateral that Lender customarily would require as security for loan facilities on its own account and risk where the permitted borrowing level is based principally on a borrowing base derived from a borrower's inventory and accounts receivable, but where such additional collateral does not enter into the borrowing base calculation.

"Permitted Liens" shall mean (a) Liens for taxes, assessments or other governmental charges or levies not delinquent, or, being contested in good faith and by appropriate proceedings and with respect to which proper reserves have been taken by Borrower; provided, that, the Lien shall have no effect on the priority of the Liens in favor of Lender or the value of the assets in which Lender has such a Lien and a stay of enforcement of any such Lien shall be in effect; (b) deposits or pledges securing obligations under worker's compensation, unemployment insurance, social security or public liability laws or similar legislation; (c) deposits or pledges securing bids, tenders, contracts (other than contracts for the payment of money), leases, statutory obligations, surety and appeal bonds and other obligations of like nature arising in the ordinary course of Borrower's business; (d) judgment Liens that have been stayed or bonded; (e) mechanics', workers', materialmen's or other like Liens arising in the ordinary course of Borrower's business with respect to obligations which are not due; (f) Liens placed upon fixed assets hereafter acquired to secure a portion of the purchase price thereof, provided, that, any such Lien shall not encumber any other property of Borrower; (g) security interests being terminated concurrently with the execution of the Loan Documents; and (h) Liens disclosed in Section 6.D. of the Loan

Authorization Agreement, provided that, except as otherwise permitted by Ex-Im Bank in writing, such Liens in Section 6.D. shall be subordinate to the Liens in favor of Lender on Primary Collateral.

"Person" shall mean any individual, sole proprietorship, partnership, limited liability partnership, joint venture, trust, unincorporated organization, association, corporation, limited liability company, institution, public benefit corporation, entity or government (whether national, federal, provincial, state, county, city, municipal or otherwise, including any instrumentality, division, agency, body or department thereof), and shall include such Person's successors and assigns.

"Pro Rata Percentage" shall mean, with respect to a Loan Facility, as of the date of determination thereof, the principal balance of the Credit Accommodations outstanding as a percentage of the combined principal balance of all loans from Lender to such Borrower including the then outstanding principal balance of the Credit Accommodations plus unfunded amounts under outstanding Letters of Credit.

"Principals" shall mean any officer, director, owner, partner, key employee, or other Person with primary management or supervisory responsibilities with respect to Borrower or any other Person (whether or not an employee) who has critical influence on or substantive control over the transactions covered by this Agreement.

"Retainage" shall mean that portion of the purchase price of an Export Order that a Buyer is not obligated to pay until the end of a specified period of time following the satisfactory performance under such Export Order.

"Retainage Accounts Receivable" shall mean those portions of Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable arising out of a Retainage.

"Retainage Value" shall mean, at the date of determination thereof, the aggregate face amount of Retainage Accounts Receivable as permitted by Ex-Im Bank in writing, less taxes, discounts, credits and allowances, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Revolving Loan Facility" shall mean the credit facility or portion thereof established by Lender in favor of Borrower for the purpose of providing working capital in the form of loans and/or Letters of Credit to finance the manufacture, production or purchase and subsequent export sale of Items pursuant to Loan Documents under which Credit Accommodations may be made and repaid on a continuous basis based solely on credit availability on the Export-Related Borrowing Base during the term of such credit facility

"Special Conditions" shall mean those conditions, if any, set forth in Section 13 of the Loan Authorization Agreement.

"Specific Export Orders" shall mean those Export Orders specified in Section 5.D. of the Loan Authorization Agreement as applicable for a Transaction Specific Revolving Loan Facility or a Transaction Specific Loan Facility.

"Standby Letters of Credit" shall mean those letters of credit subject to the ISP or UCP issued or caused to be issued by Lender for Borrower's account that can be drawn upon by a Buyer only if Borrower fails to perform all of its obligations with respect to an Export Order.

"Transaction Specific Loan Facility" shall mean a credit facility or a portion thereof established by Lender in favor of Borrower for the purpose of providing working capital in the form of loans and/or Letters of Credit to finance the manufacture, production or purchase and subsequent export sale of Items pursuant to Loan Documents under which Credit Accommodations are made based solely on credit availability on the Export-Related Borrowing Base relating to Specific Export Orders and once such Credit Accommodations are repaid they may not be reborrowed.

"Transaction Specific Revolving Loan Facility" shall mean a Revolving Credit Facility established to provide financing of Specific Export Orders.

"UCC" shall mean the Uniform Commercial Code, as the same may be in effect from time to time in the relevant United States jurisdiction.

"UCP" shall mean the Uniform Customs and Practice for Documentary Credits (1993 Revision), International Chamber of Commerce Publication No. 500 and any amendments and revisions thereof.

"U.S." or "United States" shall mean the United States of America including any division or agency thereof (including United States embassies or United States military bases located overseas), and any United States Territory (including without limitation, Puerto Rico, Guam or the United States Virgin Islands).

"U.S. Content" shall mean, with respect to any Item, all the costs, including labor, materials, services and overhead, but not markup or profit margin, which are of U.S. origin or manufacture, and which are incorporated into an Item in the United States.

"Warranty" shall mean Borrower's guarantee to Buyer that the Items will function as intended during the warranty period set forth in the applicable Export Order.

"Warranty Letter of Credit" shall mean a Standby Letter of Credit which is issued or caused to be issued by Lender to support the obligations of Borrower with respect to a Warranty or a Standby Letter of Credit which by its terms becomes a Warranty Letter of Credit.

1.02 Rules of Construction. For purposes of this Agreement, the following additional rules of construction shall apply, unless specifically indicated to the contrary: (a) wherever from the context it appears appropriate, each term stated in either the singular or plural shall include the singular and the plural, and pronouns stated in the masculine, feminine or neuter gender shall include the masculine, the feminine and the neuter; (b) the term "or" is not exclusive; (c) the term "including" (or any form thereof) shall not be limiting or exclusive; (d) all references to statutes and related regulations shall include any amendments of same and any successor statutes and regulations; (e) the words "this Agreement", "herein", "hereof", "hereunder" or other words of similar import refer to this Agreement as a whole including the schedules, exhibits, and annexes

hereto as the same may be amended, modified or supplemented; (f) all references in this Agreement to sections, schedules, exhibits, and annexes shall refer to the corresponding sections, schedules, exhibits, and annexes of or to this Agreement; and (g) all references to any instruments or agreements, including references to any of the Loan Documents, the Delegated Authority Letter Agreement, or the Fast Track Lender Agreement shall include any and all modifications, amendments and supplements thereto and any and all extensions or renewals thereof to the extent permitted under this Agreement.

1.03 Incorporation of Recitals. The Recitals to this Agreement are incorporated into and shall constitute a part of this Agreement.

ARTICLE II OBLIGATIONS OF BORROWER

Until payment in full of all Loan Facility Obligations and termination of the Loan Documents, Borrower agrees as follows:

2.01 Use of Credit Accommodations. (a) Borrower shall use Credit Accommodations only for the purpose of enabling Borrower to finance the cost of manufacturing, producing, purchasing or selling the Items. Borrower may not use any of the Credit Accommodations for the purpose of: (i) servicing or repaying any of Borrower's pre-existing or future indebtedness unrelated to the Loan Facility unless approved by Ex-Im Bank in writing; (ii) acquiring fixed assets or capital assets for use in Borrower's business; (iii) acquiring, equipping or renting commercial space outside of the United States; (iv) paying the salaries of non U.S. citizens or non-U.S. permanent residents who are located in offices outside of the United States; or (v) in connection with a Retainage or Warranty unless approved by Ex-Im Bank in writing.

(b) In addition, no Credit Accommodation may be used to finance the manufacture, purchase or sale of any of the following:

(i) Items to be sold to a Buyer located in a country as to which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;

(ii) that part of the cost of the Items which is not U.S. Content unless such part is not greater than fifty percent (50%) of the cost of the Items and is incorporated into the Items in the United States;

(iii) defense articles or defense services;

(iv) Capital Goods unless in accordance with Section 2.14 of this Agreement; or

(v) without Ex-Im Bank's prior written consent, any Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities.

2.02 Security Interests. Borrower agrees to cooperate with Lender in any steps Lender shall take to file and maintain valid, enforceable and perfected security interests in the Collateral.

2.03 Loan Documents and Loan Authorization Agreement. (a) This Agreement and each of the other Loan Documents applicable to Borrower have been duly executed and delivered on behalf of Borrower, and are and will continue to be legal and valid obligations of Borrower, enforceable against it in accordance with its terms.

(b) Borrower shall comply with all of the terms and conditions of this Agreement, the Loan Authorization Agreement and each of the other Loan Documents to which it is a party.

(c) Borrower hereby represents and warrants to Lender that Borrower is an Eligible Person.

2.04 Export-Related Borrowing Base Certificates and Export Orders. (a) In order to receive Credit Accommodations under the Loan Facility, Borrower shall have delivered to Lender an Export-Related Borrowing Base Certificate as frequently as required by Lender but at least within the past month, together with a copy of the Export Order(s) or, for Revolving Loan Facilities, if permitted by Lender, a written summary of the Export Orders (when Eligible Export-Related Inventory and Eligible Overseas Export-Related Inventory are entering the Export-Related Borrowing Base) against which Borrower is requesting Credit Accommodations. In addition, so long as there are any Credit Accommodations outstanding under the Loan Facility, Borrower shall deliver to Lender an Export-Related Borrowing Base Certificate at least once each month. Lender shall determine if daily electronic reporting reconciled monthly may substitute for monthly Export-Related Borrowing Base Certificates. If the Lender requires an Export-Related Borrowing Base Certificate more frequently, Borrower shall deliver such Export-Related Borrowing Base Certificate as required by Lender.

(b) If Lender permits summaries of Export Orders, Borrower shall also deliver promptly to Lender copies of any Export Orders requested by Lender.

2.05 Schedules, Reports and Other Statements. With the delivery of each Export-Related Borrowing Base Certificate required in Section 2.04 above, Borrower shall submit to Lender in writing (a) an Inventory schedule for the preceding month, as applicable, and (b) an Accounts Receivable Aging Report for the preceding month. Borrower shall also furnish to Lender promptly upon request such information, reports, contracts, invoices and other data concerning the Collateral as Lender may from time to time specify.

2.06 Exclusions from the Export-Related Borrowing Base. In determining the Export-Related Borrowing Base, Borrower shall exclude therefrom Inventory which are not Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory and Accounts Receivable which are not Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable. Borrower shall promptly, but in any event within five (5) Business Days, notify Lender (a) if any then existing Export-Related Inventory or Export-Related Overseas Inventory no longer constitutes Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory, as applicable or (b) of any event or circumstance which to Borrower's knowledge would cause Lender to consider any then existing Export-Related Accounts Receivable or Export-Related Overseas Accounts Receivable as no longer constituting an Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable, as applicable.

2.07 Borrowings and Reborrowings. (a) If the Loan Facility is a Revolving Loan Facility or Transaction Specific Revolving Loan Facility, provided that Borrower is not in default under any of the Loan Documents, Borrower may borrow, repay and reborrow amounts under such Loan Facility up to the credit available on the current Export-Related Borrowing Base Certificate subject to the terms of this Agreement and each of the other Loan Documents until the close of business on the Final Disbursement Date.

(b) If the Loan Facility is a Transaction Specific Loan Facility, provided that Borrower is not in default under any of the Loan Documents, Borrower may borrow (but not reborrow) amounts under the Loan Facility up to the credit available on the current Export-Related Borrowing Base Certificate subject to the terms of this Agreement and each of the other Loan Documents until the close of business on the Final Disbursement Date.

2.08 Repayment Terms. (a) The Borrower on a Revolving Loan Facility shall pay in full the outstanding Loan Facility Obligations no later than the first Business Day after the Final Disbursement Date unless such Loan Facility is renewed or extended by Lender consistent with procedures required by Ex-Im Bank.

(b) The Borrower on a Transaction Specific Loan Facility and a Transaction Specific Revolving Loan Facility shall, within two (2) Business Days of the receipt thereof, pay to Lender (for application against the outstanding Loan Facility Obligations) all checks, drafts, cash and other remittances it may receive in payment or on account of the Export-Related Accounts Receivable, Export-Related Overseas Accounts Receivable or any other Collateral, in precisely the form received (except for the endorsement of Borrower where necessary). Pending such deposit, Borrower shall hold such amounts in trust for Lender separate and apart and shall not commingle any such items of payment with any of its other funds or property. Unless a Transaction Specific Loan Facility or Transaction Specific Revolving Loan Facility is renewed or extended by Lender consistent with procedures required by Ex-Im Bank, Borrower shall pay in full all outstanding Loan Facility Obligations no later than the first Business Day after the Final Disbursement Date, except for Eligible Export-Related Accounts Receivables and Eligible Export-Related Overseas Accounts Receivable outstanding as of the Final Disbursement Date and due and payable after such date, for which the principal and accrued and unpaid interest thereon shall be due and payable no later than the first Business Day after the date such Accounts Receivable are due and payable.

2.09 Financial Statements. Borrower shall deliver to Lender the financial statements required to be delivered by Borrower in accordance with Section 11 of the Loan Authorization Agreement.

2.10 Additional Security or Payment. (a) Borrower shall at all times ensure that the Export-Related Borrowing Base equals or exceeds the aggregate outstanding amount of Disbursements. If informed by Lender or if Borrower otherwise has actual knowledge that the Export-Related Borrowing Base is at any time less than the aggregate outstanding amount of Disbursements, Borrower shall, within five (5) Business Days, either (i) furnish additional Collateral to Lender, in form and amount satisfactory to Lender and Ex-Im Bank or (ii) pay to Lender an amount equal to the difference between the aggregate outstanding amount of Disbursements and the Export-Related Borrowing Base.

(b) For purposes of this Agreement, in determining the Export-Related Borrowing Base there shall be deducted from the Export-Related Borrowing Base an amount equal to (i) twenty-five percent (25%) of the undrawn amount of outstanding Commercial Letters of Credit and Standby Letters of Credit and (ii) one hundred percent (100%) of the undrawn amount of outstanding Warranty Letters of Credit less the amount of cash collateral held by Lender to secure Warranty Letters of Credit.

(c) Unless otherwise approved in writing by Ex-Im Bank, for Revolving Loan Facilities (other than Transaction Specific Revolving Loan Facilities), Borrower shall at all times ensure that the sum of the outstanding amount of Disbursements and the undrawn amount of outstanding Commercial Letters of Credit that is supported by Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory (discounted by the relevant Advance Rate percentages) in the Export-Related Borrowing Base does not exceed sixty percent (60%) of the sum of the total outstanding amount of Disbursements and the undrawn amount of all outstanding Commercial Letters of Credit. If informed by Lender or if Borrower otherwise has actual knowledge that the sum of the outstanding amount of Disbursements and the undrawn amount of outstanding Commercial Letters of Credit that is supported by such Inventory exceeds sixty percent (60%) of the sum of the total outstanding Disbursements and the undrawn amount of all outstanding Commercial Letters of Credit, Borrower shall, within five (5) Business Days, either (i) furnish additional non-Inventory Collateral to Lender, in form and amount satisfactory to Lender and Ex-Im Bank, or (ii) pay down the applicable portion of the outstanding Disbursements or (iii) reduce the undrawn amount of outstanding Commercial Letters of Credit such that the above described ratio is not exceeded.

(d) If informed by Lender or if Borrower otherwise has actual knowledge that the conditions of Section 2.16(g) are at any time not being met, Borrower shall, within five (5) Business Days, either (i) furnish additional Collateral to Lender that is not Eligible Export-Related Overseas Accounts Receivable or Eligible Export-Related Overseas Inventory, in form and amount satisfactory to Lender and Ex-Im Bank, or (ii) remove from the Export-Related Borrowing Base the portion of Eligible Export-Related Overseas Accounts Receivable or Eligible Export-Related Overseas Inventory that supports greater than fifty percent (50%) of the Export-Related Borrowing Base.

2.11 Continued Security Interest. Borrower shall not change (a) its name or identity in any manner, (b) the location of its principal place of business or its jurisdiction of organization or formation, (c) the location of any of the Collateral or (d) the location of any of the books or records related to the Collateral, in each instance without giving thirty (30) days prior written notice thereof to Lender and taking all actions deemed necessary or appropriate by Lender to continuously protect and perfect Lender's Liens upon the Collateral.

2.12 Inspection of Collateral and Facilities. (a) Borrower shall permit the representatives of Lender and Ex-Im Bank to make at any time during normal business hours inspections of the Collateral and of Borrower's facilities, activities, and books and records, and shall cause its officers and employees to give full cooperation and assistance in connection therewith.

(b) Borrower agrees to facilitate Lender's conduct of field examinations at Borrower's facilities in accordance with the time schedule and content for such examinations

that Lender requests. Such field examinations shall address at a minimum: (x) the value of the Collateral against which Credit Accommodations may be provided, (y) the amount, if any, that the aggregate outstanding amount of Disbursements exceeds the Export-Related Borrowing Base and (z) whether such Borrower is in material compliance with the terms of each of the Loan Documents. Such field examinations shall include an inspection and evaluation of the Export-Related Inventory and Export-Related Overseas Inventory, a book audit of Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable, a review of the Accounts Receivable Aging Reports and a review of Borrower's compliance with any Special Conditions. Lenders who opt to use the Export-Related Historical Inventory Value in the Export-Related Borrowing Base calculation shall reconcile those numbers against the calculation for the relevant time periods using the Export-Related Inventory Value. Whenever Export-Related Accounts Receivable or Export-Related Inventory derived from Indirect Exports are in the Export-Related Borrowing Base, Lender shall verify compliance with Section 2.15 herein, including taking a random sampling of ultimate foreign purchasers.

2.13 General Intangibles. Borrower represents and warrants that it owns, or is licensed to use, all General Intangibles necessary to conduct its business as currently conducted except where the failure of Borrower to own or license such General Intangibles could not reasonably be expected to have a Material Adverse Effect.

2.14 Economic Impact Approval. (a) For Loan Facilities up to and including \$10 million, Borrower acknowledges that Capital Goods may not be included as Items, and Export-Related Inventory, Export-Related Overseas Inventory, Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable in connection with the sale of such Capital Goods may not be included in the Export-Related Borrowing Base, if such Capital Goods would enable a foreign buyer to establish or expand production of a product where, as of the date of the Economic Impact Certification covering such Item: (i) the Buyer is subject to a Final Anti-Dumping (AD) or Countervailing Duty (CVD) order, or a Suspension Agreement arising from a AD or CVD investigation, and such product is substantially the same as the product that is the subject of the AD/CVD order or suspension agreement; or (ii) the Buyer is the subject of a Section 201 injury determination by the International Trade Commission ("ITC") and such product is substantially the same as a product that is the subject of the ITC injury determination. Borrower may consult with Ex-Im Bank regarding the appropriate application of this Section 2.14(a) and may, at its option, request that Ex-Im Bank issue an Economic Impact Approval covering any Items listed in Section 4.A. of the Loan Authorization Agreement. For Loan Facilities over \$10 million involving Items that are Capital Goods, Borrower shall obtain from Ex-Im Bank, and abide by, an Economic Impact Approval covering all Items listed in Section 4(A) of the Loan Authorization Agreement.

(b) Borrower shall provide Lender with a certification in the form of Annex B (an "Economic Impact Certification") covering the Items stated in Section 4(A) of the Loan Authorization Agreement prior to Lender including such Items in the Loan Authorization Agreement. Prior to Lender amending the Loan Authorization Agreement to include additional Items, Borrower shall provide Lender with an additional Economic Impact Certification covering such additional Items.

2.15 Indirect Exports. Indirect Exports may be included as Items in a Loan Facility provided that funds available under such Loan Facility's Export-Related Borrowing Base

supported by Accounts Receivable and Inventory derived from Indirect Exports at no time exceed ten percent (10%) of the Maximum Amount of such Loan Facility, and provided, further that (a) the ultimate foreign buyer for the Items must be located in a country in which Ex-Im Bank is not legally prohibited from doing business in accordance with the Country Limitation Schedule, and (b) the Borrower must make available to Lender verifiable evidence of intent to export the Indirect Exports from the United States, which evidence may be contained in the Export Orders and Accounts Receivable Aging Reports and supporting documents. Lender must obtain written consent from Ex-Im Bank prior to including funds derived from Indirect Exports in an Export-Related Borrowing Base above the ten percent (10%) threshold.

2.16 Overseas Inventory and Accounts Receivable. Upon the prior written consent of Ex-Im Bank, Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory of a Borrower or of an Affiliated Foreign Person (as defined below) may be included in the Export-Related Borrowing Base provided that conditions required by Ex-Im Bank, including the following, are met:

- (a) the Affiliated Foreign Person, if any, has been approved by Ex-Im Bank;
- (b) the Affiliated Foreign Person, if any, is a Borrower under the relevant Loan Facility;
- (c) notwithstanding the Maximum Amount of the Loan Facility, all payments due and payable on such Export-Related Overseas Accounts Receivable are collected through a cash collateral account under Lender's control;
- (d) as of the Effective Date, or such later date when the Export-Related Overseas Accounts Receivable and/or Export-Related Overseas Inventory are added to the Loan Facility, Lender has obtained a valid and enforceable first priority Lien in the Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory, as applicable;
- (e) as of the Effective Date, or such later date when the Export-Related Overseas Accounts Receivable and/or Export-Related Overseas Inventory are added to the Loan Facility, Lender has obtained a legal opinion confirming the security interest in the Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory;
- (f) the Export-Related Overseas Accounts Receivable are due and payable in United States Dollars or other currency acceptable to Ex-Im Bank; and
- (g) at no time may the portion of the Export-Related Borrowing Base derived from Eligible Export-Related Overseas Accounts Receivable and Eligible Export-Related Overseas Inventory exceed fifty percent (50%) of the Export-Related Borrowing Base.

For purposes hereof, an "Affiliated Foreign Person" shall mean a subsidiary or affiliate of a Borrower on the same Loan Facility, which has duly executed as a Borrower all of the applicable Loan Documents and any other documents required by Ex-Im Bank, meets all of the requirements of the definition of Eligible Person other than subclause (a) thereof and is in good standing in the country of its formation or otherwise authorized to conduct business in such country.

2.17 Country Limitation Schedule. Unless otherwise informed in writing by Lender or Ex-Im Bank, Borrower shall be entitled to rely on the last copy of the Country Limitation Schedule distributed from Lender to Borrower.

2.18 Notice of Certain Events. Borrower shall promptly, but in any event within five (5) Business Days, notify Lender in writing of the occurrence of any of the following:

(a) Borrower or any Guarantor (i) applies for, consents to or suffers the appointment of, or the taking of possession by, a receiver, custodian, trustee, liquidator or similar fiduciary of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have dismissed within thirty (30) days, any petition filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;

(b) any Lien in any of the Collateral, granted or intended by the Loan Documents to be granted to Lender, ceases to be a valid, enforceable, perfected, first priority Lien (or a lesser priority if expressly permitted pursuant to Section 6 of the Loan Authorization Agreement) subject only to Permitted Liens;

(c) the issuance of any levy, assessment, attachment, seizure or Lien, other than a Permitted Lien, against any of the Collateral which is not stayed or lifted within thirty (30) calendar days;

(d) any proceeding is commenced by or against Borrower or any Guarantor for the liquidation of its assets or dissolution;

(e) any litigation is filed against Borrower or any Guarantor which has had or could reasonably be expected to have a Material Adverse Effect and such litigation is not withdrawn or dismissed within thirty (30) calendar days of the filing thereof;

(f) any default or event of default under the Loan Documents;

(g) any failure to comply with any terms of the Loan Authorization Agreement;

(h) any material provision of this Agreement or any other Loan Document for any reason ceases to be valid, binding and enforceable in accordance with its terms;

(i) any event which has had or could reasonably be expected to have a Material Adverse Effect; or

(j) the aggregate outstanding amount of Disbursements exceeds the applicable Export-Related Borrowing Base.

2.19 Insurance. Borrower will at all times carry property, liability and other insurance, with insurers acceptable to Lender, in such form and amounts, and with such deductibles and other provisions, as Lender shall require, and Borrower will provide evidence of such insurance to Lender on the proper Acord Form, so that Lender is satisfied that such insurance is, at all times, in full force and effect. Each property insurance policy shall name Lender as loss payee or mortgagee and shall contain a lender's loss payable endorsement in form acceptable to Lender and each liability insurance policy shall name Lender as an additional insured. All policies of insurance shall provide that they may not be cancelled or changed without at least thirty (30) days' prior written notice to Lender and shall otherwise be in form and substance satisfactory to Lender. Borrower will promptly deliver to Lender copies of all reports made to insurance companies.

2.20 Taxes. Borrower has timely filed all tax returns and reports required by applicable law, has timely paid all applicable taxes, assessments, deposits and contributions owing by Borrower and will timely pay all such items in the future as they become due and payable. Borrower may, however, defer payment of any contested taxes; provided, that Borrower (a) in good faith contests Borrower's obligation to pay such taxes by appropriate proceedings promptly and diligently instituted and conducted; (b) notifies Lender in writing of the commencement of, and any material development in, the proceedings; (c) posts bonds or takes any other steps required to keep the contested taxes from becoming a Lien upon any of the Collateral; and (d) maintains adequate reserves therefore in conformity with GAAP.

2.21 Compliance with Laws. Borrower represents and warrants that it has complied in all material respects with all provisions of all applicable laws and regulations, including those relating to Borrower's ownership of real or personal property, the conduct and licensing of Borrower's business, the payment and withholding of taxes, ERISA and other employee matters, safety and environmental matters.

2.22 Negative Covenants. Without the prior written consent of Ex-Im Bank and Lender, Borrower shall not: (a) merge, consolidate or otherwise combine with any other Person; (b) acquire all or substantially all of the assets or capital stock of any other Person; (c) sell, lease, transfer, convey, assign or otherwise dispose of any of its assets, except for the sale of Inventory in the ordinary course of business and the disposition of obsolete equipment in the ordinary course of business; (d) create any Lien on the Collateral except for Permitted Liens; (e) make any material changes in its organizational structure or identity; or (f) enter into any agreement to do any of the foregoing.

2.23 Cross Default. Borrower shall be deemed in default under the Loan Facility if Borrower fails to pay when due any amount payable to Lender under any loan or other credit accommodations to Borrower whether or not guaranteed by Ex-Im Bank.

2.24 Munitions List. If any of the Items are articles, services, or related technical data that are listed on the United States Munitions List (part 121 of title 22 of the Code of Federal Regulations), Borrower shall send a written notice promptly, but in any event within five (5) Business Days, of Borrower learning thereof to Lender describing the Items(s) and the corresponding invoice amount.

2.25 Suspension and Debarment, etc. On the date of this Agreement neither Borrower nor its Principals are (a) debarred, suspended, proposed for debarment with a final determination still pending, declared ineligible or voluntarily excluded (as such terms are defined under any of the Debarment Regulations referred to below) from participating in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations or (b) indicted, convicted or had a civil judgment rendered against Borrower or any of its Principals for any of the offenses listed in any of the Debarment Regulations. Unless authorized by Ex-Im Bank, Borrower will not knowingly enter into any transactions in connection with the Items with any person who is debarred, suspended, declared ineligible or voluntarily excluded from participation in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations. Borrower will provide immediate written notice to Lender if at any time it learns that the certification set forth in this Section 2.24 was erroneous when made or has become erroneous by reason of changed circumstances.

ARTICLE III RIGHTS AND REMEDIES

3.01 Indemnification. Upon Ex-Im Bank's payment of a Claim to Lender in connection with the Loan Facility pursuant to the Master Guarantee Agreement, Ex-Im Bank may assume all rights and remedies of Lender under the Loan Documents and may enforce any such rights or remedies against Borrower, the Collateral and any Guarantors. Borrower shall hold Ex-Im Bank and Lender harmless from and indemnify them against any and all liabilities, damages, claims, costs and losses incurred or suffered by either of them resulting from (a) any materially incorrect certification or statement knowingly made by Borrower or its agent to Ex-Im Bank or Lender in connection with the Loan Facility, this Agreement, the Loan Authorization Agreement or any other Loan Documents or (b) any material breach by Borrower of the terms and conditions of this Agreement, the Loan Authorization Agreement or any of the other Loan Documents. Borrower also acknowledges that any statement, certification or representation made by Borrower in connection with the Loan Facility is subject to the penalties provided in Article 18 U.S.C. Section 1001.

3.02 Liens. Borrower agrees that any and all Liens granted by it to Lender are also hereby granted to Ex-Im Bank to secure Borrower's obligation, however arising, to reimburse Ex-Im Bank for any payments made by Ex-Im Bank pursuant to the Master Guarantee Agreement. Lender is authorized to apply the proceeds of, and recoveries from, any property subject to such Liens to the satisfaction of Loan Facility Obligations in accordance with the terms of any agreement between Lender and Ex-Im Bank.

**ARTICLE IV
MISCELLANEOUS**

4.01 Governing Law. This Agreement and the obligations arising under this Agreement shall be governed by, and construed in accordance with, the law of the state governing the Loan Agreement.

4.02 Notification. All notices required by this Agreement shall be given in the manner and to the parties provided for in the Loan Agreement.

4.03 Partial Invalidity. If at any time any of the provisions of this Agreement becomes illegal, invalid or unenforceable in any respect under the law of any jurisdiction, neither the legality, the validity nor the enforceability of the remaining provisions hereof shall in any way be affected or impaired.

4.04 Waiver of Jury Trial. BORROWER HEREBY KNOWINGLY, VOLUNTARILY AND INTENTIONALLY WAIVES ANY AND ALL RIGHTS IT MAY HAVE TO A TRIAL BY JURY IN RESPECT OF ANY ACTION, SUIT, PROCEEDING OR OTHER LITIGATION BROUGHT TO RESOLVE ANY DISPUTE ARISING UNDER, ARISING OUT OF OR IN CONNECTION WITH THIS AGREEMENT, THE LOAN AUTHORIZATION AGREEMENT, ANY LOAN DOCUMENT, OR ANY OTHER AGREEMENT, DOCUMENT OR INSTRUMENT EXECUTED OR DELIVERED IN CONNECTION HERewith OR THEREWITH OR ANY COURSE OF CONDUCT, COURSE OF DEALING, STATEMENTS (WHETHER VERBAL OR WRITTEN), OR ACTIONS OR OMISSIONS OF LENDER, EX-IM BANK, OR ANY OTHER PERSON, RELATING TO THIS AGREEMENT, THE LOAN AUTHORIZATION AGREEMENT OR ANY OTHER LOAN DOCUMENT.

4.05 Consequential Damages. Neither Ex-Im Bank, Lender nor any agent or attorney for any of them shall be liable to Borrower for consequential damages arising from any breach of contract, tort or other wrong relating to the establishment, administration or collection of the Loan Facility Obligations.

IN WITNESS WHEREOF, Borrower has caused this Agreement to be duly executed as the 6th day of March, 2018.

BL ACQUISITION CORP.
(Name of Borrower)

By: /s/ John R. Beaver
(Signature)

Name: John R. Beaver
(Print or Type)

Title: SVP and Chief Financial Officer
(Print or Type)

ACKNOWLEDGED:
WESTERN ALLIANCE BANK
(Name of Lender)

By: /s/ Brenda Penrod
(Signature)

Name: Brenda Penrod
(Print or Type)

Title: Vice President
(Print or Type)

ANNEXES:

- Annex A - Loan Authorization Agreement, Fast Track Loan Authorization Agreement or
Loan Authorization Notice, as applicable
- Annex B - Economic Impact Certification

CONSENT OF GUARANTORS

Each of the undersigned as a Guarantor of the obligations of Borrower to the Lender executing the foregoing Agreement hereby agrees that the foregoing Agreement, each of their respective Guarantee Agreements and each other Loan Documents may be assigned to the Export-Import Bank of the United States.

[INDIVIDUAL GUARANTOR]

[CORPORATE GUARANTOR]

B y : _____
N a m e : _____
Title: _____

**EXPORT-IMPORT BANK OF THE UNITED STATES WORKING
CAPITAL GUARANTEE PROGRAM**

BORROWER AGREEMENT

Ex-Im Bank 12/31/05

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**EXPORT-IMPORT BANK OF THE UNITED STATES WORKING
CAPITAL GUARANTEE PROGRAM BORROWER
AGREEMENT**

THIS BORROWER AGREEMENT (this "Agreement") is made and entered into by the entity identified as Borrower on the signature page hereof ("Borrower") in favor of the Export-Import Bank of the United States ("Ex-Im Bank") and the institution identified as Lender on the signature page hereof ("Lender").

RECITALS

Borrower has requested that Lender establish a Loan Facility in favor of Borrower for the purposes of providing Borrower with working capital to finance the manufacture, production or purchase and subsequent export sale of Items.

Lender and Borrower expect that Ex-Im Bank will provide a guarantee to Lender regarding this Loan Facility subject to the terms and conditions of the Master Guarantee Agreement, a Loan Authorization Agreement, and to the extent applicable, the Delegated Authority Letter Agreement or Fast Track Lender Agreement.

Lender and Ex-Im Bank have requested that Borrower execute this Agreement as a condition precedent to Lender establishing the Loan Facility and Ex-Im Bank providing the guarantee.

NOW, THEREFORE, Borrower hereby agrees as follows:

**ARTICLE I
DEFINITIONS**

1.01 Definition of Terms. As used in this Agreement, including the Recitals to this Agreement and the Loan Authorization Agreement, the following terms shall have the following meanings:

"Accounts Receivable" shall mean all of Borrower's now owned or hereafter acquired (a) "accounts" (as such term is defined in the UCC), other receivables, book debts and other forms of obligations, whether arising out of goods sold or services rendered or from any other transaction; (b) rights in, to and under all purchase orders or receipts for goods or services; (c) rights to any goods represented or purported to be represented by any of the foregoing (including unpaid sellers' rights of rescission, replevin, reclamation and stoppage in transit and rights to returned, reclaimed or repossessed goods); (d) moneys due or to become due to such Borrower under all purchase orders and contracts (which includes Export Orders) for the sale of goods or the performance of services or both by Borrower (whether or not yet earned by performance on the part of Borrower), including the proceeds of the foregoing; (e) any notes, drafts, letters of credit, insurance proceeds or other instruments, documents and writings evidencing or supporting the foregoing; and (f) all collateral security and guarantees of any kind given by any other Person with respect to any of the foregoing.

“Accounts Receivable Aging Report” shall mean a report detailing the Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable for a Loan Facility, and the applicable terms for the relevant time period; in the case of Indirect Exports, such report shall indicate the portion of such Accounts Receivables corresponding to Indirect Exports.

"Advance Rate" shall mean, with respect to a Loan Facility, the rate specified in Section 5.C. of the Loan Authorization Agreement for each category of Primary Collateral except for Export-Related General Intangibles and Other Collateral. Unless otherwise set forth in writing by Ex-Im Bank, in no event shall the Advance Rate exceed (i) ninety percent (90%) for Eligible Export-Related Accounts Receivable, (ii) seventy five percent (75%) for Eligible Export-Related Inventory, (iii) seventy percent (70%) for Eligible Export-Related Overseas Accounts Receivable or (iv) sixty percent (60%) for Eligible Export-Related Overseas Inventory and (v) twenty five percent (25%) for Retainage Accounts Receivable.

“Affiliated Foreign Person” shall have the meaning set forth in Section 2.15.

"Business Day" shall mean any day on which the Federal Reserve Bank of New York is open for business.

"Buyer" shall mean a Person that has entered into one or more Export Orders with Borrower or who is an obligor on Export-Related Accounts Receivable or Export-Related Overseas Accounts Receivable.

“Capital Good” shall mean a capital good (e.g., manufacturing equipment, licensing agreements) that will establish or expand foreign production capacity of an exportable good.

"Collateral" shall mean all real and personal property and interest in real and personal property in or upon which Lender has been, or shall be, granted a Lien as security for the payment of all the Loan Facility Obligations and all products and proceeds (cash and non-cash) thereof.

"Commercial Letters of Credit" shall mean those letters of credit subject to the UCP payable in Dollars and issued or caused to be issued by Lender on behalf of Borrower under a Loan Facility for the benefit of a supplier(s) of Borrower in connection with Borrower's purchase of goods or services from the supplier in support of the export of the Items.

"Country Limitation Schedule" shall mean the schedule published from time to time by Ex-Im Bank setting forth on a country by country basis whether and under what conditions ExIm Bank will provide coverage for the financing of export transactions to countries listed therein.

“Credit Accommodation Amount” shall mean, the sum of (a) the aggregate outstanding amount of Disbursements and (b) the aggregate outstanding Letter of Credit Obligations, which sum may not exceed the Maximum Amount.

"Credit Accommodations" shall mean, collectively, Disbursements and Letter of Credit Obligations.

"Debarment Regulations" shall mean, collectively, (a) the Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 53 Fed. Reg. 19204 (May 26, 1988), (b) Subpart 9.4 (Debarment, Suspension, and Ineligibility) of the Federal Acquisition Regulations, 48 C.F.R. 9.400-9.409 and (c) the revised Governmentwide Debarment and Suspension (Nonprocurement) regulations (Common Rule), 60 Fed. Reg. 33037 (June 26, 1995).

"Delegated Authority Letter Agreement" shall mean the Delegated Authority Letter Agreement, if any, between Ex-Im Bank and Lender.

"Disbursement" shall mean, collectively, (a) an advance of a working capital loan from Lender to Borrower under the Loan Facility, and (b) an advance to fund a drawing under a Letter of Credit issued or caused to be issued by Lender for the account of Borrower under the Loan Facility.

"Dollars" or "\$" shall mean the lawful currency of the United States.

"Economic Impact Approval" shall mean a written approval issued by Ex-Im Bank stating the conditions under which a Capital Good may be included as an Item in a Loan Facility consistent with Ex-Im Bank's economic impact procedures (or other mechanism for making this determination that Ex-Im Bank notifies Lender of in writing).

"Economic Impact Certification" shall have the meaning set forth in Section 2.14(b).

"Effective Date" shall mean the date on which (a) all of the Loan Documents have been executed by Lender, Borrower and, if applicable, Ex-Im Bank and (b) all of the conditions to the making of the initial Credit Accommodations under the Loan Documents or any amendments thereto have been satisfied.

"Eligible Export-Related Accounts Receivable" shall mean Export-Related Accounts Receivable which are acceptable to Lender and which are deemed to be eligible pursuant to the Loan Documents, but in no event shall Eligible Export-Related Accounts Receivable include any Account Receivable:

- (a) that does not arise from the sale of Items in the ordinary course of Borrower's business;
- (b) that is not subject to a valid, perfected first priority Lien in favor of Lender;
- (c) as to which any covenant, representation or warranty contained in the Loan Documents with respect to such Account Receivable has been breached;
- (d) that is not owned by Borrower or is subject to any right, claim or interest of another Person other than the Lien in favor of Lender;
- (e) with respect to which an invoice has not been sent;
- (f) that arises from the sale of defense articles or defense services;

(g) that arises from the sale of Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities unless with Ex-Im Bank's prior written consent;

(h) that is due and payable from a Buyer located in a country with which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;

(i) that does not comply with the requirements of the Country Limitation Schedule;

(j) that is due and payable more than one hundred eighty (180) days from the date of the invoice;

(k) that is not paid within sixty (60) calendar days from its original due date, unless it is insured through Ex-Im Bank export credit insurance for comprehensive commercial and political risk, or through Ex-Im Bank approved private insurers for comparable coverage, in which case it is not paid within ninety (90) calendar days from its due date;

(l) of a Buyer for whom fifty percent (50%) or more of the Accounts Receivable of such Buyer do not satisfy the requirements of subclauses (j) and (k) above;

(m) that arises from a sale of goods to or performance of services for an employee of Borrower, a stockholder of Borrower, a subsidiary of Borrower, a Person with a controlling interest in Borrower or a Person which shares common controlling ownership with Borrower;

(n) that is backed by a letter of credit unless the Items covered by the subject letter of credit have been shipped;

(o) that Lender or Ex-Im Bank, in its reasonable judgment, deems uncollectible for any reason;

(p) that is due and payable in a currency other than Dollars, except as may be approved in writing by Ex-Im Bank;

(q) that is due and payable from a military Buyer, except as may be approved in writing by Ex-Im Bank;

(r) that does not comply with the terms of sale set forth in Section 7 of the Loan Authorization Agreement;

(s) that is due and payable from a Buyer who (i) applies for, suffers, or consents to the appointment of, or the taking of possession by, a receiver, custodian, trustee or liquidator of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have dismissed, any petition which is filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;

(t) that arises from a bill-and-hold, guaranteed sale, sale-and-return, sale on approval, consignment or any other repurchase or return basis or is evidenced by chattel paper;

(u) for which the Items giving rise to such Accounts Receivable have not been shipped to the Buyer or when the Items are services, such services have not been performed or when the Export Order specifies a timing for invoicing the Items other than shipment or performance and the Items have not been invoiced in accordance with such terms of the Export Order, or the Accounts Receivable otherwise do not represent a final sale;

(v) that is subject to any offset, deduction, defense, dispute, or counterclaim or the Buyer is also a creditor or supplier of Borrower or the Account Receivable is contingent in any respect or for any reason;

(w) for which Borrower has made any agreement with the Buyer for any deduction therefrom, except for discounts or allowances made in the ordinary course of business for prompt payment, all of which discounts or allowances are reflected in the calculation of the face value of each respective invoice related thereto;

(x) for which any of the Items giving rise to such Account Receivable have been returned, rejected or repossessed;

(y) that is included as an eligible receivable under any other credit facility to which Borrower is a party;

(z) any of the Items giving rise to such Accounts Receivable are Capital Goods, unless the transaction is in accordance with Section 2.14;

(aa) that is due and payable from a Buyer that is, or is located in, the United States; provided however, that this subsection (aa) shall not preclude an Export-Related Accounts Receivable arising from the sale of Items to foreign contractors or subcontractors providing services to a United States Embassy or the United States Military located overseas from being deemed an Eligible Export-Related Accounts Receivable; or

(bb) that arises from the sale of Items that do not meet the U.S. Content requirements in accordance with Section 2.01(b) (ii).

"Eligible Export-Related Inventory" shall mean Export-Related Inventory which is acceptable to Lender and which is deemed to be eligible pursuant to the Loan Documents, but in no event shall Eligible Export-Related Inventory include any Inventory:

- (a) that is not subject to a valid, perfected first priority Lien in favor of Lender;
- (b) that is located at an address that has not been disclosed to Lender in writing;
- (c) that is placed by Borrower on consignment or held by Borrower on consignment from another Person;
- (d) that is in the possession of a processor or bailee, or located on premises leased or subleased to Borrower, or on premises subject to a mortgage in favor of a Person other than Lender, unless such processor or bailee or mortgagee or the lessor or sublessor of such premises, as the case may be, has executed and delivered all documentation which Lender shall require to evidence the subordination or other limitation or extinguishment of such Person's rights with respect to such Inventory and Lender's right to gain access thereto;
- (e) that is produced in violation of the Fair Labor Standards Act or subject to the "hot goods" provisions contained in 29 U.S.C. §215 or any successor statute or section;
- (f) as to which any covenant, representation or warranty with respect to such Inventory contained in the Loan Documents has been breached;
- (g) that is not located in the United States unless expressly permitted by Lender, on terms acceptable to Lender;
- (h) that is an Item or is to be incorporated into Items that do not meet U.S. Content requirements in accordance with Section 2.01(b)(ii);
- (i) that is demonstration Inventory;
- (j) that consists of proprietary software (i.e. software designed solely for Borrower's internal use and not intended for resale);
- (k) that is damaged, obsolete, returned, defective, recalled or unfit for further processing;
- (l) that has been previously exported from the United States;
- (m) that constitutes, or will be incorporated into Items that constitute, defense articles or defense services;
- (n) that is an Item or will be incorporated into Items that will be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities unless with Ex-Im Bank's prior written consent;

(o) that is an Item or is to be incorporated into Items destined for shipment to a country as to which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;

(p) that is an Item or is to be incorporated into Items destined for shipment to a Buyer located in a country in which Ex-Im Bank coverage is not available for commercial reasons as designated in the Country Limitation Schedule, unless and only to the extent that such Items are to be sold to such country on terms of a letter of credit confirmed by a bank acceptable to Ex-Im Bank;

(q) that constitutes, or is to be incorporated into, Items whose sale would result in an Accounts Receivable which would not be an Eligible Export-Related Accounts Receivable;

(r) that is included as eligible inventory under any other credit facility to which Borrower is a party; or

(s) that is, or is to be incorporated into, an Item that is a Capital Good, unless the transaction is in accordance with Section 2.14.

"Eligible Export-Related Overseas Accounts Receivable" shall mean Export-Related Overseas Accounts Receivable which are acceptable to Lender and which are deemed to be eligible pursuant to the Loan Documents but in no event shall include the Accounts Receivable (a) through (bb) excluded from the definition of Eligible Export-Related Accounts Receivable.

"Eligible Export-Related Overseas Inventory" shall mean Export-Related Overseas Inventory which is acceptable to Lender and which is deemed to be eligible pursuant to the Loan Documents, but in no event shall include the Inventory (a) through (r) excluded from the definition of Eligible Export-Related Inventory.

"Eligible Person" shall mean a sole proprietorship, partnership, limited liability partnership, corporation or limited liability company which (a) is domiciled, organized or formed, as the case may be, in the United States, whether or not such entity is owned by a foreign national or foreign entity; (b) is in good standing in the state of its formation or otherwise authorized to conduct business in the United States; (c) is not currently suspended or debarred from doing business with the United States government or any instrumentality, division, agency or department thereof; (d) exports or plans to export Items; (e) operates and has operated as a going concern for at least one (1) year; (f) has a positive tangible net worth determined in accordance with GAAP; and (g) has revenue generating operations relating to its core business activities for at least one year. An Affiliated Foreign Person that meets all of the requirements of the foregoing definition of Eligible Person other than subclause (a) thereof shall be deemed to be an Eligible Person

"ERISA" shall mean the Employee Retirement Income Security Act of 1974 and the rules and regulations promulgated thereunder

"Export Order" shall mean a documented purchase order or contract evidencing a Buyer's agreement to purchase the Items from Borrower for export from the United States, which documentation shall include written information that is necessary to confirm such purchase order or contract, including identification of the Items, the name of the Buyer, the country of destination, contact information for the Buyer and the total amount of the purchase order or contract; in the case of Indirect Exports, such documentation shall further include a copy of the written purchase order or contract from a foreign purchaser or other documentation clearly evidencing a foreign purchaser's agreement to purchase the Items.

"Export-Related Accounts Receivable" shall mean those Accounts Receivable arising from the sale of Items which are due and payable to Borrower in the United States. "Export-Related Accounts Receivable Value" shall mean, at the date of determination thereof, the aggregate face amount of Eligible Export-Related Accounts Receivable less taxes, discounts, credits, allowances and Retainages, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Export-Related Borrowing Base" shall mean, at the date of determination thereof, the sum of (a) (if Lender elects to include) the Export-Related Inventory Value or Export-Related Historical Inventory Value multiplied by the Advance Rate applicable to Eligible Export-Related Inventory set forth in Section 5.B.(1.) of the Loan Authorization Agreement, plus (b) the Export-Related Accounts Receivable Value multiplied by the Advance Rate applicable to Eligible Export-Related Accounts Receivable set forth in Section 5.B.(2.) of the Loan Authorization Agreement, plus (c) if permitted by Ex-Im Bank in writing, the Retainage Value multiplied by the Advance Rate applicable to Retainages set forth in Section 5.B.(3.) of the Loan Authorization Agreement, plus (d) the Other Assets set forth in Section 5.B.(4.) of the Loan Authorization Agreement multiplied by the Advance Rate agreed to in writing by Ex-Im Bank, plus (e) if permitted by Ex-Im Bank in writing, the Export-Related Overseas Accounts Receivable Value multiplied by the Advance Rate applicable to Eligible Export-Related Overseas Accounts Receivable set forth in Section 5.B.(5.) of the Loan Authorization Agreement, plus (f) if permitted by Ex-Im Bank in writing, the Export-Related Overseas Inventory Value multiplied by the Advance Rate applicable to Eligible Export-Related Overseas Inventory set forth in Section 5.B.(6.) of the Loan Authorization Agreement, less (g) the amounts required to be reserved pursuant to Sections 4.12 and 4.13 of this Agreement for each outstanding Letter of Credit, less (h) such reserves and in such amounts deemed necessary and proper by Lender from time to time.

"Export-Related Borrowing Base Certificate" shall mean a certificate in the form provided or approved by Lender, executed by Borrower and delivered to Lender pursuant to the Loan Documents detailing the Export-Related Borrowing Base supporting the Credit Accommodations which reflects, to the extent included in the Export-Related Borrowing Base, Export-Related Accounts Receivable, Eligible Export-Related Accounts Receivable, Export-Related Inventory, Eligible Export-Related Inventory, Export-Related Overseas Accounts Receivable, Eligible Export-Related Accounts Receivable, Export-Related Overseas Inventory and Eligible Export-Related Overseas Inventory balances that have been reconciled with Borrower's general ledger, Accounts Receivable Aging Report and Inventory schedule.

"Export-Related General Intangibles" shall mean the Pro Rata Percentage of General Intangibles determined as of the earlier of: (i) the date such General Intangibles are liquidated and (ii) the date Borrower fails to pay when due any outstanding amount of principal or accrued interest payable under the Loan Documents that becomes the basis for a Payment Default on which a Claim is filed.

"Export-Related Historical Inventory Value" shall mean with respect to a Borrower, the relevant Export-Related Sales Ratio multiplied by the lowest of (i) the cost of such Borrower's Inventory as determined in accordance with GAAP, or (ii) the market value of such Borrower's Inventory as determined in accordance with GAAP or (iii) the appraised or orderly liquidation value of such Borrower's Inventory, if Lender has loans and financial accommodations to such Borrower for which it conducts (or contracts for the performance of) such an appraised or orderly liquidation value. "Export-Related Inventory" shall mean the Inventory of Borrower located in the United States that has been purchased, manufactured or otherwise acquired by Borrower for sale or resale as Items, or to be incorporated into Items to be sold or resold pursuant to Export Orders.

"Export-Related Inventory Value" shall mean, at the date of determination thereof, the lowest of (i) the cost of Eligible Exported-Related Inventory as determined in accordance with GAAP, or (ii) the market value of Eligible Export-Related Inventory as determined in accordance with GAAP or (iii) the lower of the appraised market value or orderly liquidation value of the Eligible Export-Related Inventory, if Lender has other loans and financial accommodations to a Borrower for which it conducts (or contracts for the performance of) such an appraised or orderly liquidation value.

"Export-Related Overseas Accounts Receivable" shall mean those Accounts Receivable arising from the sale of Items which are due and payable outside of the United States either to a Borrower or an Affiliated Foreign Person.

"Export-Related Overseas Accounts Receivable Value" shall mean, with respect to a Loan Facility, at the date of determination thereof, the aggregate face amount of Eligible Export-Related Overseas Accounts Receivable less taxes, discounts, credits, allowances and Retainages, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Export-Related Overseas Inventory" shall mean the Inventory of Borrower located outside of the United States that has been purchased, manufactured or otherwise acquired by such Borrower for sale or resale as Items, or to be incorporated into Items to be sold or resold pursuant to Export Orders.

"Export-Related Overseas Inventory Value" shall mean, at the date of determination thereof, the lowest of (i) the cost of Eligible Export-Related Overseas Inventory as determined in accordance with GAAP, (ii) the market value of Eligible Export-Related Overseas Inventory as determined in accordance with GAAP or (iii) the appraised or orderly liquidation value of the Eligible Export-Related Overseas Inventory, if Lender has other loans and financial accommodations to Borrower or an Affiliated Foreign Person for which it conducts (or contracts for the performance of) such a appraised or orderly liquidation.

“Export-Related Sales Ratio” shall mean with respect to a Borrower, the percentage of such Borrower’s total sales revenue derived from the sale of Eligible Export-Related Inventory over a rolling twelve-month period ending no more than ninety (90) days prior to the date of the relevant Export-Related Borrowing Base Certificate

"Extension" shall mean, with respect to a Loan Facility, an amendment to the Loan Authorization Agreement extending the Final Disbursement Date on the same terms and conditions as the Loan Facility for an aggregate period not to exceed one hundred and twenty (120) days beyond the original Final Disbursement Date, either as agreed to in writing by Ex-Im Bank or, in the case of Delegated Authority, as notified by Lender to Ex-Im Bank pursuant to its authority under the Delegated Authority Letter Agreement. “Fast Track Lender Agreement” shall mean the Fast Track Lender Agreement, if any, between Ex-Im Bank and Lender.

"Final Disbursement Date" shall mean the last date on which Lender may make a Disbursement set forth in Section 10 of the Loan Authorization Agreement (including as amended by an Extension) or, if such date is not a Business Day, the next succeeding Business Day; provided, however, to the extent that Lender has not received cash collateral in the amount of the Letter of Credit Obligations or an equivalent full indemnity from Borrower or Guarantor, as applicable, with respect to Letter of Credit Obligations outstanding on the Final Disbursement Date, the Final Disbursement Date with respect to an advance to fund a drawing under such Letter of Credit shall be no later than thirty (30) days after any such drawing which may be no later than the expiry date of the Letter of Credit related thereto.

"GAAP" shall mean the generally accepted accounting principles issued in the United States.

"General Intangibles" shall mean all intellectual property and other "general intangibles" (as such term is defined in the UCC).

"Guarantor" shall mean any Person which is identified in Section 3 of the Loan Authorization Agreement who shall guarantee (jointly and severally if more than one) the payment and performance of all or a portion of the Loan Facility Obligations.

"Guarantee Agreement" shall mean a valid and enforceable agreement of guarantee executed by each Guarantor in favor of Lender.

“Indirect Exports” shall mean finished goods or services that are sold by a Borrower to a Buyer located in the United States, are intended for export from the United States, and are identified in Section 4.A.(2.) of the Loan Authorization Agreement.

"Inventory" shall mean all "inventory" (as such term is defined in the UCC), now or hereafter owned or acquired by Borrower, wherever located, including all inventory, merchandise, goods and other personal property which are held by or on behalf of Borrower for sale or lease or are furnished or are to be furnished under a contract of service or which constitute raw materials, work in process or materials used or consumed or to be used or consumed in Borrower's business or in the processing, production, packaging, promotion, delivery or shipping of the same, including other supplies.

"ISP" shall mean the International Standby Practices-ISP98, International Chamber of Commerce Publication No. 590 and any amendments and revisions thereof.

"Issuing Bank" shall mean the bank that issues a Letter of Credit, which bank is Lender itself or a bank that Lender has caused to issue a Letter of Credit by way of a guarantee or reimbursement obligation.

"Items" shall mean the finished goods or services which are intended for export from the United States, either directly or as an Indirect Export, meet the U.S. Content requirements in accordance with Section 2.01(b)(ii) of this Agreement and are specified in Section 4.A. of the Loan Authorization Agreement.

"Letter of Credit" shall mean a Commercial Letter of Credit or a Standby Letter of Credit.

"Letter of Credit Obligations" shall mean all undrawn amounts of outstanding obligations incurred by Lender, whether direct or indirect, contingent or otherwise, due or not due, in connection with the issuance or guarantee by Lender or Issuing Bank of Letters of Credit.

"Lien" shall mean any mortgage, security deed or deed of trust, pledge, hypothecation, assignment, deposit arrangement, lien, charge, claim, security interest, security title, easement or encumbrance, or preference, priority or other security agreement or preferential arrangement of any kind or nature whatsoever (including any lease or title retention agreement, any financing lease having substantially the same economic effect as any of the foregoing, and the filing of, or agreement to give, any financing statement perfecting a security interest under the UCC or comparable law of any jurisdiction) by which property is encumbered or otherwise charged.

"Loan Agreement" shall mean a valid and enforceable agreement between Lender and a Borrower setting forth, with respect to each Loan Facility, the terms and conditions of such Loan Facility.

"Loan Authorization Agreement" shall mean, as applicable, the duly executed Loan Authorization Agreement, Fast Track Loan Authorization Agreement, or the Loan Authorization Notice, setting forth certain terms and conditions of each Loan Facility, a copy of which is attached hereto as Annex A.

"Loan Authorization Notice" shall mean the Loan Authorization Notice executed by Lender and delivered to Ex-Im Bank in accordance with the Delegated Authority Letter Agreement setting forth the terms and conditions of each Loan Facility.

"Loan Documents" shall mean the Loan Authorization Agreement, the Loan Agreement, this Agreement, each promissory note (if applicable), each Guarantee Agreement, and all other instruments, agreements and documents now or hereafter executed by the applicable Borrower, any Guarantor, Lender or Ex-Im Bank evidencing, securing, guaranteeing or otherwise relating to the Loan Facility or any Credit Accommodations made thereunder.

"Loan Facility" shall mean the Revolving Loan Facility, the Transaction Specific Loan Facility or the Transaction Specific Revolving Loan Facility established by Lender in favor of Borrower under the Loan Documents.

"Loan Facility Obligations" shall mean all loans, advances, debts, expenses, fees, liabilities, and obligations, including any accrued interest thereon, for the performance of covenants, tasks or duties or for payment of monetary amounts (whether or not such performance is then required or contingent, or amounts are liquidated or determinable) owing by Borrower to Lender, of any kind or nature, present or future, arising in connection with the Loan Facility. "Loan Facility Term" shall mean, with respect to a Loan Facility, the number of months or portion thereof from the Effective Date to the Final Disbursement Date as set forth in the Loan Authorization Agreement as amended.

"Master Guarantee Agreement" shall mean the Master Guarantee Agreement between Ex-Im Bank and Lender, as amended, modified, supplemented and restated from time to time.

"Material Adverse Effect" shall mean a material adverse effect on (a) the business, assets, operations, prospects or financial or other condition of Borrower or any Guarantor, (b) any Borrower's ability to pay or perform the Loan Facility Obligations in accordance with the terms thereof, (c) the Collateral or Lender's Liens on the Collateral or the priority of such Lien, or (d) Lender's rights and remedies under the Loan Documents.

"Maximum Amount" shall mean the maximum Credit Accommodation Amount that may be outstanding at any time under each Loan Facility, as specified in Section 5.A. of the Loan Authorization Agreement.

"Other Assets" shall mean, with respect to a Loan Facility, such other assets of a Borrower to be included in Primary Collateral, which may include cash and marketable securities, or such other assets as Ex-Im Bank agrees to in writing, and disclosed as Primary Collateral in Section 6.A. of the Loan Authorization Agreement. The applicable Advance Rate (to be multiplied by the Other Asset Value) shall be as agreed to by Ex-Im Bank in writing case by case and set forth in Section 5.B.(4) of the Loan Authorization Agreement.

"Other Asset Value" shall mean, with respect to a Loan Facility, at the date of determination thereof, the value of the Other Assets as determined in accordance with GAAP.

"Other Collateral" shall mean any additional collateral that Lender customarily would require as security for loan facilities on its own account and risk where the permitted borrowing level is based principally on a borrowing base derived from a borrower's inventory and accounts receivable, but where such additional collateral does not enter into the borrowing base calculation.

"Permitted Liens" shall mean (a) Liens for taxes, assessments or other governmental charges or levies not delinquent, or, being contested in good faith and by appropriate proceedings and with respect to which proper reserves have been taken by Borrower; provided, that, the Lien shall have no effect on the priority of the Liens in favor of Lender or the value of the assets in which Lender has such a Lien and a stay of enforcement of any such Lien shall be in effect; (b) deposits or pledges securing obligations under worker's compensation, unemployment insurance, social security or public liability laws or similar legislation; (c) deposits or pledges securing bids, tenders, contracts (other than contracts for the payment of money), leases, statutory obligations, surety and appeal bonds and other obligations of like nature arising in the ordinary course

of Borrower's business; (d) judgment Liens that have been stayed or bonded; (e) mechanics', workers', materialmen's or other like Liens arising in the ordinary course of Borrower's business with respect to obligations which are not due; (f) Liens placed upon fixed assets hereafter acquired to secure a portion of the purchase price thereof, provided, that, any such Lien shall not encumber any other property of Borrower; (g) security interests being terminated concurrently with the execution of the Loan Documents; and (h) Liens disclosed in Section 6.D. of the Loan Authorization Agreement, provided that, except as otherwise permitted by Ex-Im Bank in writing, such Liens in Section 6.D. shall be subordinate to the Liens in favor of Lender on Primary Collateral.

"Person" shall mean any individual, sole proprietorship, partnership, limited liability partnership, joint venture, trust, unincorporated organization, association, corporation, limited liability company, institution, public benefit corporation, entity or government (whether national, federal, provincial, state, county, city, municipal or otherwise, including any instrumentality, division, agency, body or department thereof), and shall include such Person's successors and assigns.

"Pro Rata Percentage" shall mean, with respect to a Loan Facility, as of the date of determination thereof, the principal balance of the Credit Accommodations outstanding as a percentage of the combined principal balance of all loans from Lender to such Borrower including the then outstanding principal balance of the Credit Accommodations plus unfunded amounts under outstanding Letters of Credit.

"Principals" shall mean any officer, director, owner, partner, key employee, or other Person with primary management or supervisory responsibilities with respect to Borrower or any other Person (whether or not an employee) who has critical influence on or substantive control over the transactions covered by this Agreement.

"Retainage" shall mean that portion of the purchase price of an Export Order that a Buyer is not obligated to pay until the end of a specified period of time following the satisfactory performance under such Export Order.

"Retainage Accounts Receivable" shall mean those portions of Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable arising out of a Retainage.

"Retainage Value" shall mean, at the date of determination thereof, the aggregate face amount of Retainage Accounts Receivable as permitted by Ex-Im Bank in writing, less taxes, discounts, credits and allowances, except to the extent otherwise permitted by Ex-Im Bank in writing.

"Revolving Loan Facility" shall mean the credit facility or portion thereof established by Lender in favor of Borrower for the purpose of providing working capital in the form of loans and/or Letters of Credit to finance the manufacture, production or purchase and subsequent export sale of Items pursuant to Loan Documents under which Credit Accommodations may be made and repaid on a continuous basis based solely on credit availability on the Export-Related Borrowing Base during the term of such credit facility

"Special Conditions" shall mean those conditions, if any, set forth in Section 13 of the Loan Authorization Agreement.

"Specific Export Orders" shall mean those Export Orders specified in Section 5.D. of the Loan Authorization Agreement as applicable for a Transaction Specific Revolving Loan Facility or a Transaction Specific Loan Facility. "Standby Letters of Credit" shall mean those letters of credit subject to the ISP or UCP issued or caused to be issued by Lender for Borrower's account that can be drawn upon by a Buyer only if Borrower fails to perform all of its obligations with respect to an Export Order.

"Transaction Specific Loan Facility" shall mean a credit facility or a portion thereof established by Lender in favor of Borrower for the purpose of providing working capital in the form of loans and/or Letters of Credit to finance the manufacture, production or purchase and subsequent export sale of Items pursuant to Loan Documents under which Credit Accommodations are made based solely on credit availability on the Export-Related Borrowing Base relating to Specific Export Orders and once such Credit Accommodations are repaid they may not be reborrowed.

"Transaction Specific Revolving Loan Facility" shall mean a Revolving Credit Facility established to provide financing of Specific Export Orders.

"UCC" shall mean the Uniform Commercial Code, as the same may be in effect from time to time in the relevant United States jurisdiction.

"UCP" shall mean the Uniform Customs and Practice for Documentary Credits (1993 Revision), International Chamber of Commerce Publication No. 500 and any amendments and revisions thereof.

"U.S." or "United States" shall mean the United States of America including any division or agency thereof (including United States embassies or United States military bases located overseas), and any United States Territory (including without limitation, Puerto Rico, Guam or the United States Virgin Islands).

"U.S. Content" shall mean, with respect to any Item, all the costs, including labor, materials, services and overhead, but not markup or profit margin, which are of U.S. origin or manufacture, and which are incorporated into an Item in the United States.

"Warranty" shall mean Borrower's guarantee to Buyer that the Items will function as intended during the warranty period set forth in the applicable Export Order.

"Warranty Letter of Credit" shall mean a Standby Letter of Credit which is issued or caused to be issued by Lender to support the obligations of Borrower with respect to a Warranty or a Standby Letter of Credit which by its terms becomes a Warranty Letter of Credit.

1.02 Rules of Construction. For purposes of this Agreement, the following additional rules of construction shall apply, unless specifically indicated to the contrary: (a) wherever from the context it appears appropriate, each term stated in either the singular or plural shall include the singular and the plural, and pronouns stated in the masculine, feminine or neuter gender shall include the masculine, the feminine and the neuter; (b) the term "or" is not exclusive; (c) the term "including" (or any form thereof) shall not be limiting or exclusive; (d) all references to statutes and related regulations shall include any amendments of same and any successor statutes and regulations; (e) the words "this Agreement", "herein", "hereof", "hereunder" or other words of similar import refer to this Agreement as a whole including the schedules, exhibits, and annexes hereto as the same may be amended, modified or supplemented; (f) all references in this Agreement to sections, schedules, exhibits, and annexes shall refer to the corresponding sections, schedules, exhibits, and annexes of or to this Agreement; and (g) all references to any instruments or agreements, including references to any of the Loan Documents, the Delegated Authority Letter Agreement, or the Fast Track Lender Agreement shall include any and all modifications, amendments and supplements thereto and any and all extensions or renewals thereof to the extent permitted under this Agreement.

1.03 Incorporation of Recitals. The Recitals to this Agreement are incorporated into and shall constitute a part of this Agreement.

ARTICLE II OBLIGATIONS OF BORROWER

Until payment in full of all Loan Facility Obligations and termination of the Loan Documents, Borrower agrees as follows:

2.01 Use of Credit Accommodations. (a) Borrower shall use Credit Accommodations only for the purpose of enabling Borrower to finance the cost of manufacturing, producing, purchasing or selling the Items. Borrower may not use any of the Credit Accommodations for the purpose of: (i) servicing or repaying any of Borrower's pre-existing or future indebtedness unrelated to the Loan Facility unless approved by Ex-Im Bank in writing; (ii) acquiring fixed assets or capital assets for use in Borrower's business; (iii) acquiring, equipping or renting commercial space outside of the United States; (iv) paying the salaries of non U.S. citizens or non-U.S. permanent residents who are located in offices outside of the United States; or (v) in connection with a Retainage or Warranty unless approved by Ex-Im Bank in writing.

(b) In addition, no Credit Accommodation may be used to finance the manufacture, purchase or sale of any of the following:

(i) Items to be sold to a Buyer located in a country as to which Ex-Im Bank is prohibited from doing business as designated in the Country Limitation Schedule;

(ii) that part of the cost of the Items which is not U.S. Content unless such part is not greater than fifty percent (50%) of the cost of the Items and is incorporated into the Items in the United States;

(iii) defense articles or defense services;

(iv) Capital Goods unless in accordance with Section 2.14 of this Agreement; or

(v) without Ex-Im Bank's prior written consent, any Items to be used in the construction, alteration, operation or maintenance of nuclear power, enrichment, reprocessing, research or heavy water production facilities.

2.02 Security Interests. Borrower agrees to cooperate with Lender in any steps Lender shall take to file and maintain valid, enforceable and perfected security interests in the Collateral.

2.03 Loan Documents and Loan Authorization Agreement. (a) This Agreement and each of the other Loan Documents applicable to Borrower have been duly executed and delivered on behalf of Borrower, and are and will continue to be legal and valid obligations of Borrower, enforceable against it in accordance with its terms.

(b) Borrower shall comply with all of the terms and conditions of this Agreement, the Loan Authorization Agreement and each of the other Loan Documents to which it is a party.

(c) Borrower hereby represents and warrants to Lender that Borrower is an Eligible Person.

2.04 Export-Related Borrowing Base Certificates and Export Orders. (a) In order to receive Credit Accommodations under the Loan Facility, Borrower shall have delivered to Lender an Export-Related Borrowing Base Certificate as frequently as required by Lender but at least within the past month, together with a copy of the Export Order(s) or, for Revolving Loan Facilities, if permitted by Lender, a written summary of the Export Orders (when Eligible Export-Related Inventory and Eligible Overseas Export-Related Inventory are entering the Export-Related Borrowing Base) against which Borrower is requesting Credit Accommodations. In addition, so long as there are any Credit Accommodations outstanding under the Loan Facility, Borrower shall deliver to Lender an Export-Related Borrowing Base Certificate at least once each month. Lender shall determine if daily electronic reporting reconciled monthly may substitute for monthly Export-Related Borrowing Base Certificates. If the Lender requires an Export-Related Borrowing Base Certificate more frequently, Borrower shall deliver such Export-Related Borrowing Base Certificate as required by Lender.

(b) If Lender permits summaries of Export Orders, Borrower shall also deliver promptly to Lender copies of any Export Orders requested by Lender.

2.05 Schedules, Reports and Other Statements. With the delivery of each Export-Related Borrowing Base Certificate required in Section 2.04 above, Borrower shall submit to Lender in writing (a) an Inventory schedule for the preceding month, as applicable, and (b) an Accounts Receivable Aging Report for the preceding month. Borrower shall also furnish to Lender promptly upon request such information, reports, contracts, invoices and other data concerning the Collateral as Lender may from time to time specify.

2.06 Exclusions from the Export-Related Borrowing Base. In determining the Export-Related Borrowing Base, Borrower shall exclude therefrom Inventory which are not Eligible

Export-Related Inventory or Eligible Export-Related Overseas Inventory and Accounts Receivable which are not Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable. Borrower shall promptly, but in any event within five (5) Business Days, notify Lender (a) if any then existing Export-Related Inventory or Export-Related Overseas Inventory no longer constitutes Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory, as applicable or (b) of any event or circumstance which to Borrower's knowledge would cause Lender to consider any then existing Export-Related Accounts Receivable or Export-Related Overseas Accounts Receivable as no longer constituting an Eligible Export-Related Accounts Receivable or Eligible Export-Related Overseas Accounts Receivable, as applicable.

2.07 Borrowings and Reborrowings. (a) If the Loan Facility is a Revolving Loan Facility or Transaction Specific Revolving Loan Facility, provided that Borrower is not in default under any of the Loan Documents, Borrower may borrow, repay and reborrow amounts under such Loan Facility up to the credit available on the current Export-Related Borrowing Base Certificate subject to the terms of this Agreement and each of the other Loan Documents until the close of business on the Final Disbursement Date.

(b) If the Loan Facility is a Transaction Specific Loan Facility, provided that Borrower is not in default under any of the Loan Documents, Borrower may borrow (but not reborrow) amounts under the Loan Facility up to the credit available on the current Export-Related Borrowing Base Certificate subject to the terms of this Agreement and each of the other Loan Documents until the close of business on the Final Disbursement Date.

2.08 Repayment Terms. (a) The Borrower on a Revolving Loan Facility shall pay in full the outstanding Loan Facility Obligations no later than the first Business Day after the Final Disbursement Date unless such Loan Facility is renewed or extended by Lender consistent with procedures required by Ex-Im Bank.

(b) The Borrower on a Transaction Specific Loan Facility and a Transaction Specific Revolving Loan Facility shall, within two (2) Business Days of the receipt thereof, pay to Lender (for application against the outstanding Loan Facility Obligations) all checks, drafts, cash and other remittances it may receive in payment or on account of the Export-Related Accounts Receivable, Export-Related Overseas Accounts Receivable or any other Collateral, in precisely the form received (except for the endorsement of Borrower where necessary). Pending such deposit, Borrower shall hold such amounts in trust for Lender separate and apart and shall not commingle any such items of payment with any of its other funds or property. Unless a Transaction Specific Loan Facility or Transaction Specific Revolving Loan Facility is renewed or extended by Lender consistent with procedures required by Ex-Im Bank, Borrower shall pay in full all outstanding Loan Facility Obligations no later than the first Business Day after the Final Disbursement Date, except for Eligible Export-Related Accounts Receivables and Eligible Export-Related Overseas Accounts Receivable outstanding as of the Final Disbursement Date and due and payable after such date, for which the principal and accrued and unpaid interest thereon shall be due and payable no later than the first Business Day after the date such Accounts Receivable are due and payable.

2.09 Financial Statements. Borrower shall deliver to Lender the financial statements required to be delivered by Borrower in accordance with Section 11 of the Loan Authorization Agreement.

2.10 Additional Security or Payment. (a) Borrower shall at all times ensure that the Export-Related Borrowing Base equals or exceeds the aggregate outstanding amount of Disbursements. If informed by Lender or if Borrower otherwise has actual knowledge that the Export-Related Borrowing Base is at any time less than the aggregate outstanding amount of Disbursements, Borrower shall, within five (5) Business Days, either (i) furnish additional Collateral to Lender, in form and amount satisfactory to Lender and Ex-Im Bank or (ii) pay to Lender an amount equal to the difference between the aggregate outstanding amount of Disbursements and the Export-Related Borrowing Base.

(b) For purposes of this Agreement, in determining the Export-Related Borrowing Base there shall be deducted from the Export-Related Borrowing Base an amount equal to (i) twenty-five percent (25%) of the undrawn amount of outstanding Commercial Letters of Credit and Standby Letters of Credit and (ii) one hundred percent (100%) of the undrawn amount of outstanding Warranty Letters of Credit less the amount of cash collateral held by Lender to secure Warranty Letters of Credit.

(c) Unless otherwise approved in writing by Ex-Im Bank, for Revolving Loan Facilities (other than Transaction Specific Revolving Loan Facilities), Borrower shall at all times ensure that the sum of the outstanding amount of Disbursements and the undrawn amount of outstanding Commercial Letters of Credit that is supported by Eligible Export-Related Inventory or Eligible Export-Related Overseas Inventory (discounted by the relevant Advance Rate percentages) in the Export-Related Borrowing Base does not exceed sixty percent (60%) of the sum of the total outstanding amount of Disbursements and the undrawn amount of all outstanding Commercial Letters of Credit. If informed by Lender or if Borrower otherwise has actual knowledge that the sum of the outstanding amount of Disbursements and the undrawn amount of outstanding Commercial Letters of Credit that is supported by such Inventory exceeds sixty percent (60%) of the sum of the total outstanding Disbursements and the undrawn amount of all outstanding Commercial Letters of Credit, Borrower shall, within five (5) Business Days, either (i) furnish additional non-Inventory Collateral to Lender, in form and amount satisfactory to Lender and Ex-Im Bank, or (ii) pay down the applicable portion of the outstanding Disbursements or (iii) reduce the undrawn amount of outstanding Commercial Letters of Credit such that the above described ratio is not exceeded.

(d) If informed by Lender or if Borrower otherwise has actual knowledge that the conditions of Section 2.16(g) are at any time not being met, Borrower shall, within five (5) Business Days, either (i) furnish additional Collateral to Lender that is not Eligible Export-Related Overseas Accounts Receivable or Eligible Export-Related Overseas Inventory, in form and amount satisfactory to Lender and Ex-Im Bank, or (ii) remove from the Export-Related Borrowing Base the portion of Eligible Export-Related Overseas Accounts Receivable or Eligible Export-Related Overseas Inventory that supports greater than fifty percent (50%) of the Export-Related Borrowing Base.

2.11 Continued Security Interest. Borrower shall not change (a) its name or identity in any manner, (b) the location of its principal place of business or its jurisdiction of organization or formation, (c) the location of any of the Collateral or (d) the location of any of the books or records related to the Collateral, in each instance without giving thirty (30) days prior written notice thereof to Lender and taking all actions deemed necessary or appropriate by Lender to continuously protect and perfect Lender's Liens upon the Collateral.

2.12 Inspection of Collateral and Facilities. (a) Borrower shall permit the representatives of Lender and Ex-Im Bank to make at any time during normal business hours inspections of the Collateral and of Borrower's facilities, activities, and books and records, and shall cause its officers and employees to give full cooperation and assistance in connection therewith.

(b) Borrower agrees to facilitate Lender's conduct of field examinations at Borrower's facilities in accordance with the time schedule and content for such examinations that Lender requests. Such field examinations shall address at a minimum: (x) the value of the Collateral against which Credit Accommodations may be provided, (y) the amount, if any, that the aggregate outstanding amount of Disbursements exceeds the Export-Related Borrowing Base and (z) whether such Borrower is in material compliance with the terms of each of the Loan Documents. Such field examinations shall include an inspection and evaluation of the Export-Related Inventory and Export-Related Overseas Inventory, a book audit of Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable, a review of the Accounts Receivable Aging Reports and a review of Borrower's compliance with any Special Conditions. Lenders who opt to use the Export-Related Historical Inventory Value in the Export-Related Borrowing Base calculation shall reconcile those numbers against the calculation for the relevant time periods using the Export-Related Inventory Value. Whenever Export-Related Accounts Receivable or Export-Related Inventory derived from Indirect Exports are in the Export-Related Borrowing Base, Lender shall verify compliance with Section 2.15 herein, including taking a random sampling of ultimate foreign purchasers.

2.13 General Intangibles. Borrower represents and warrants that it owns, or is licensed to use, all General Intangibles necessary to conduct its business as currently conducted except where the failure of Borrower to own or license such General Intangibles could not reasonably be expected to have a Material Adverse Effect.

2.14 Economic Impact Approval. (a) For Loan Facilities up to and including \$10 million, Borrower acknowledges that Capital Goods may not be included as Items, and Export-Related Inventory, Export-Related Overseas Inventory, Export-Related Accounts Receivable and Export-Related Overseas Accounts Receivable in connection with the sale of such Capital Goods may not be included in the Export-Related Borrowing Base, if such Capital Goods would enable a foreign buyer to establish or expand production of a product where, as of the date of the Economic Impact Certification covering such Item: (i) the Buyer is subject to a Final Anti-Dumping (AD) or Countervailing Duty (CVD) order, or a Suspension Agreement arising from a AD or CVD investigation, and such product is substantially the same as the product that is the subject of the AD/CVD order or suspension agreement; or (ii) the Buyer is the subject of a Section 201 injury determination by the International Trade Commission ("ITC") and such product is substantially the same as a product that is the subject of the ITC injury determination.

Borrower may consult with Ex-Im Bank regarding the appropriate application of this Section 2.14(a) and may, at its option, request that Ex-Im Bank issue an Economic Impact Approval covering any Items listed in Section 4.A. of the Loan Authorization Agreement. For Loan Facilities over \$10 million involving Items that are Capital Goods, Borrower shall obtain from Ex-Im Bank, and abide by, an Economic Impact Approval covering all Items listed in Section 4(A) of the Loan Authorization Agreement.

(b) Borrower shall provide Lender with a certification in the form of Annex B (an “Economic Impact Certification”) covering the Items stated in Section 4(A) of the Loan Authorization Agreement prior to Lender including such Items in the Loan Authorization Agreement. Prior to Lender amending the Loan Authorization Agreement to include additional Items, Borrower shall provide Lender with an additional Economic Impact Certification covering such additional Items.

2.15 Indirect Exports. Indirect Exports may be included as Items in a Loan Facility provided that funds available under such Loan Facility’s Export-Related Borrowing Base supported by Accounts Receivable and Inventory derived from Indirect Exports at no time exceed ten percent (10%) of the Maximum Amount of such Loan Facility, and provided, further that (a) the ultimate foreign buyer for the Items must be located in a country in which Ex-Im Bank is not legally prohibited from doing business in accordance with the Country Limitation Schedule, and (b) the Borrower must make available to Lender verifiable evidence of intent to export the Indirect Exports from the United States, which evidence may be contained in the Export Orders and Accounts Receivable Aging Reports and supporting documents. Lender must obtain written consent from Ex-Im Bank prior to including funds derived from Indirect Exports in an Export-Related Borrowing Base above the ten percent (10%) threshold.

2.16 Overseas Inventory and Accounts Receivable. Upon the prior written consent of Ex-Im Bank, Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory of a Borrower or of an Affiliated Foreign Person (as defined below) may be included in the Export-Related Borrowing Base provided that conditions required by Ex-Im Bank, including the following, are met:

- (a) the Affiliated Foreign Person, if any, has been approved by Ex-Im Bank;
- (b) the Affiliated Foreign Person, if any, is a Borrower under the relevant Loan Facility;
- (c) notwithstanding the Maximum Amount of the Loan Facility, all payments due and payable on such Export-Related Overseas Accounts Receivable are collected through a cash collateral account under Lender’s control;
- (d) as of the Effective Date, or such later date when the Export-Related Overseas Accounts Receivable and/or Export-Related Overseas Inventory are added to the Loan Facility, Lender has obtained a valid and enforceable first priority Lien in the Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory, as applicable;
- (e) as of the Effective Date, or such later date when the Export-Related Overseas

Accounts Receivable and/or Export-Related Overseas Inventory are added to the Loan Facility, Lender has obtained a legal opinion confirming the security interest in the Export-Related Overseas Accounts Receivable and Export-Related Overseas Inventory;

(f) the Export-Related Overseas Accounts Receivable are due and payable in United States Dollars or other currency acceptable to Ex-Im Bank; and

(g) at no time may the portion of the Export-Related Borrowing Base derived from Eligible Export-Related Overseas Accounts Receivable and Eligible Export-Related Overseas Inventory exceed fifty percent (50%) of the Export-Related Borrowing Base.

For purposes hereof, an "Affiliated Foreign Person" shall mean a subsidiary or affiliate of a Borrower on the same Loan Facility, which has duly executed as a Borrower all of the applicable Loan Documents and any other documents required by Ex-Im Bank, meets all of the requirements of the definition of Eligible Person other than subclause (a) thereof and is in good standing in the country of its formation or otherwise authorized to conduct business in such country.

2.17 Country Limitation Schedule. Unless otherwise informed in writing by Lender or Ex-Im Bank, Borrower shall be entitled to rely on the last copy of the Country Limitation Schedule distributed from Lender to Borrower.

2.18 Notice of Certain Events. Borrower shall promptly, but in any event within five (5) Business Days, notify Lender in writing of the occurrence of any of the following:

(a) Borrower or any Guarantor (i) applies for, consents to or suffers the appointment of, or the taking of possession by, a receiver, custodian, trustee, liquidator or similar fiduciary of itself or of all or a substantial part of its property or calls a meeting of its creditors, (ii) admits in writing its inability, or is generally unable, to pay its debts as they become due or ceases operations of its present business, (iii) makes a general assignment for the benefit of creditors, (iv) commences a voluntary case under any state or federal bankruptcy laws (as now or hereafter in effect), (v) is adjudicated as bankrupt or insolvent, (vi) files a petition seeking to take advantage of any other law providing for the relief of debtors, (vii) acquiesces to, or fails to have dismissed within thirty (30) days, any petition filed against it in any involuntary case under such bankruptcy laws, or (viii) takes any action for the purpose of effecting any of the foregoing;

(b) any Lien in any of the Collateral, granted or intended by the Loan Documents to be granted to Lender, ceases to be a valid, enforceable, perfected, first priority Lien (or a lesser priority if expressly permitted pursuant to Section 6 of the Loan Authorization Agreement) subject only to Permitted Liens;

(c) the issuance of any levy, assessment, attachment, seizure or Lien, other than a Permitted Lien, against any of the Collateral which is not stayed or lifted within thirty (30) calendar days;

(d) any proceeding is commenced by or against Borrower or any Guarantor for the liquidation of its assets or dissolution;

(e) any litigation is filed against Borrower or any Guarantor which has had or could

reasonably be expected to have a Material Adverse Effect and such litigation is not withdrawn or dismissed within thirty (30) calendar days of the filing thereof;

- (f) any default or event of default under the Loan Documents;
- (g) any failure to comply with any terms of the Loan Authorization Agreement;
- (h) any material provision of this Agreement or any other Loan Document for any reason ceases to be valid, binding and enforceable in accordance with its terms;
- (i) any event which has had or could reasonably be expected to have a Material Adverse Effect; or
- (j) the aggregate outstanding amount of Disbursements exceeds the applicable Export-Related Borrowing Base.

2.19 Insurance. Borrower will at all times carry property, liability and other insurance, with insurers acceptable to Lender, in such form and amounts, and with such deductibles and other provisions, as Lender shall require, and Borrower will provide evidence of such insurance to Lender on the proper Acord Form, so that Lender is satisfied that such insurance is, at all times, in full force and effect. Each property insurance policy shall name Lender as loss payee or mortgagee and shall contain a lender's loss payable endorsement in form acceptable to Lender and each liability insurance policy shall name Lender as an additional insured. All policies of insurance shall provide that they may not be cancelled or changed without at least thirty (30) days' prior written notice to Lender and shall otherwise be in form and substance satisfactory to Lender. Borrower will promptly deliver to Lender copies of all reports made to insurance companies.

2.20 Taxes. Borrower has timely filed all tax returns and reports required by applicable law, has timely paid all applicable taxes, assessments, deposits and contributions owing by Borrower and will timely pay all such items in the future as they became due and payable. Borrower may, however, defer payment of any contested taxes; provided, that Borrower (a) in good faith contests Borrower's obligation to pay such taxes by appropriate proceedings promptly and diligently instituted and conducted; (b) notifies Lender in writing of the commencement of, and any material development in, the proceedings; (c) posts bonds or takes any other steps required to keep the contested taxes from becoming a Lien upon any of the Collateral; and (d) maintains adequate reserves therefore in conformity with GAAP.

2.21 Compliance with Laws. Borrower represents and warrants that it has complied in all material respects with all provisions of all applicable laws and regulations, including those relating to Borrower's ownership of real or personal property, the conduct and licensing of Borrower's business, the payment and withholding of taxes, ERISA and other employee matters, safety and environmental matters.

2.22 Negative Covenants. Without the prior written consent of Ex-Im Bank and Lender, Borrower shall not: (a) merge, consolidate or otherwise combine with any other Person; (b) acquire all or substantially all of the assets or capital stock of any other Person; (c) sell, lease, transfer, convey, assign or otherwise dispose of any of its assets, except for the sale of Inventory

in the ordinary course of business and the disposition of obsolete equipment in the ordinary course of business; (d) create any Lien on the Collateral except for Permitted Liens; (e) make any material changes in its organizational structure or identity; or (f) enter into any agreement to do any of the foregoing.

2.23 Cross Default. Borrower shall be deemed in default under the Loan Facility if Borrower fails to pay when due any amount payable to Lender under any loan or other credit accommodations to Borrower whether or not guaranteed by Ex-Im Bank.

2.24 Munitions List. If any of the Items are articles, services, or related technical data that are listed on the United States Munitions List (part 121 of title 22 of the Code of Federal Regulations), Borrower shall send a written notice promptly, but in any event within five (5) Business Days, of Borrower learning thereof to Lender describing the Items(s) and the corresponding invoice amount

2.25 Suspension and Debarment, etc. On the date of this Agreement neither Borrower nor its Principals are (a) debarred, suspended, proposed for debarment with a final determination still pending, declared ineligible or voluntarily excluded (as such terms are defined under any of the Debarment Regulations referred to below) from participating in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations or (b) indicted, convicted or had a civil judgment rendered against Borrower or any of its Principals for any of the offenses listed in any of the Debarment Regulations. Unless authorized by Ex-Im Bank, Borrower will not knowingly enter into any transactions in connection with the Items with any person who is debarred, suspended, declared ineligible or voluntarily excluded from participation in procurement or nonprocurement transactions with any United States federal government department or agency pursuant to any of the Debarment Regulations. Borrower will provide immediate written notice to Lender if at any time it learns that the certification set forth in this Section 2.24 was erroneous when made or has become erroneous by reason of changed circumstances.

ARTICLE III RIGHTS AND REMEDIES

3.01 Indemnification. Upon Ex-Im Bank's payment of a Claim to Lender in connection with the Loan Facility pursuant to the Master Guarantee Agreement, Ex-Im Bank may assume all rights and remedies of Lender under the Loan Documents and may enforce any such rights or remedies against Borrower, the Collateral and any Guarantors. Borrower shall hold Ex-Im Bank and Lender harmless from and indemnify them against any and all liabilities, damages, claims, costs and losses incurred or suffered by either of them resulting from (a) any materially incorrect certification or statement knowingly made by Borrower or its agent to Ex-Im Bank or Lender in connection with the Loan Facility, this Agreement, the Loan Authorization Agreement or any other Loan Documents or (b) any material breach by Borrower of the terms and conditions of this Agreement, the Loan Authorization Agreement or any of the other Loan Documents. Borrower also acknowledges that any statement, certification or representation made by Borrower in connection with the Loan Facility is subject to the penalties provided in Article 18 U.S.C. Section 1001.

3.02 Liens. Borrower agrees that any and all Liens granted by it to Lender are also hereby granted to Ex-Im Bank to secure Borrower's obligation, however arising, to reimburse Ex-Im Bank for any payments made by Ex-Im Bank pursuant to the Master Guarantee Agreement. Lender is authorized to apply the proceeds of, and recoveries from, any property subject to such Liens to the satisfaction of Loan Facility Obligations in accordance with the terms of any agreement between Lender and Ex-Im Bank.

**ARTICLE IV
MISCELLANEOUS**

4.01 Governing Law. This Agreement and the obligations arising under this Agreement shall be governed by, and construed in accordance with, the law of the state governing the Loan Agreement.

4.02 Notification. All notices required by this Agreement shall be given in the manner and to the parties provided for in the Loan Agreement.

4.03 Partial Invalidity. If at any time any of the provisions of this Agreement becomes illegal, invalid or unenforceable in any respect under the law of any jurisdiction, neither the legality, the validity nor the enforceability of the remaining provisions hereof shall in any way be affected or impaired.

4.04 Waiver of Jury Trial. BORROWER HEREBY KNOWINGLY, VOLUNTARILY AND INTENTIONALLY WAIVES ANY AND ALL RIGHTS IT MAY HAVE TO A TRIAL BY JURY IN RESPECT OF ANY ACTION, SUIT, PROCEEDING OR OTHER LITIGATION BROUGHT TO RESOLVE ANY DISPUTE ARISING UNDER, ARISING OUT OF OR IN CONNECTION WITH THIS AGREEMENT, THE LOAN AUTHORIZATION AGREEMENT, ANY LOAN DOCUMENT, OR ANY OTHER AGREEMENT, DOCUMENT OR INSTRUMENT EXECUTED OR DELIVERED IN CONNECTION HERewith OR THEREWITH OR ANY COURSE OF CONDUCT, COURSE OF DEALING, STATEMENTS (WHETHER VERBAL OR WRITTEN), OR ACTIONS OR OMISSIONS OF LENDER, EX-IM BANK, OR ANY OTHER PERSON, RELATING TO THIS AGREEMENT, THE LOAN AUTHORIZATION AGREEMENT OR ANY OTHER LOAN DOCUMENT.

4.05 Consequential Damages. Neither Ex-Im Bank, Lender nor any agent or attorney for any of them shall be liable to Borrower for consequential damages arising from any breach of contract, tort or other wrong relating to the establishment, administration or collection of the Loan Facility Obligations.

IN WITNESS WHEREOF, Borrower has caused this Agreement to be duly executed as the 6th day of March, 2018.

BL ACQUISITION II INC.
(NAME OF BORROWER)

By: /s/ John R. Beaver
(Signature)

Name: John R. Beaver
(Print or Type)

Title: SVP and Chief Financial Officer
(Print or Type)

ACKNOWLEDGED:
WESTERN ALLIANCE BANK
(Name of Lender)

By: /s/ Brenda Penrod
(Signature)

Name: Brenda Penrod
(Print or Type)

Title: Vice President
(Print or Type)

ANNEXES:

- Annex A - Loan Authorization Agreement, Fast Track Loan Authorization Agreement or
Loan Authorization Notice, as applicable
- Annex B - Economic Impact Certification

CONSENT OF GUARANTORS

Each of the undersigned as a Guarantor of the obligations of Borrower to the Lender executing the foregoing Agreement hereby agrees that the foregoing Agreement, each of their respective Guarantee Agreements and each other Loan Documents may be assigned to the Export-Import Bank of the United States.

[INDIVIDUAL GUARANTOR]

[CORPORATE GUARANTOR]

B y : _____

N a m e : _____

Title:

Subsidiaries

BL Acquisition II, Inc. (Delaware)
BL Acquisition Corp. (Delaware)
Biolase International, LLC. (Delaware)
Oculase, Inc. (Delaware)

Biolase Australia, Pty. Ltd. (AUSTRALIA)
Biolase Europe, GmbH (GERMANY)
Biolase Spain, S.L. (SPAIN)
Societe Endo Technic, Inc. (FRANCE)
Biolase India Private Limited (INDIA)

Consent of Independent Registered Public Accounting Firm

BIOLASE, Inc.
Irvine, California

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (Nos. 333-194889, 333-144095, 333-112173, 333-130677, 333-177339, 333-204059, and 333-150105) and Form S-3 (Nos. 333-222564, 333-219406, 333-106260, 333-200623, 333-198291, 333-166145, 333-190158, 333-193426, 333-214281, 333-175664, 333-141417, 333-106260, 333-106290, 333-89692, and 333-58329) of BIOLASE, Inc. of our report dated March 14, 2018, relating to the consolidated financial statements and consolidated financial statement schedule of BIOLASE, Inc., which appear in this Form 10-K. Our report contains an explanatory paragraph regarding the Company's ability to continue as a going concern.

/s/ BDO USA, LLP

Costa Mesa, California
March 14, 2018

CERTIFICATION

I, Harold C. Flynn, Jr., certify that:

1. I have reviewed this Annual Report on Form 10-K for the period ended December 31, 2017 of BIOLASE, Inc.;
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 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 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.

Date: March 14, 2018

By: /s/ HAROLD C. FLYNN, JR.
Harold C. Flynn, Jr.
President and Chief Executive Officer
(Principal Executive Officer)

CERTIFICATION

I, John R. Beaver, certify that:

1. I have reviewed this Annual Report on Form 10-K for the period ended December 31, 2017 of BIOLASE, Inc.;
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 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 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.

Date: March 14, 2018

By: /s/ JOHN R. BEAVER

John R. Beaver
Senior Vice President and Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

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

In connection with the Annual Report of BIOLASE, Inc. (the "Company") on Form 10-K for the year ended December 31, 2017, (the "Report"), I, Harold C. Flynn, Jr., President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (i) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 14, 2018

By: /s/ HAROLD C. FLYNN, JR.
Harold C. Flynn, Jr.
President and Chief Executive Officer
(Principal Executive Officer)

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

In connection with the Annual Report of BIOLASE, Inc. (the "Company") on Form 10-K for the year ended December 31, 2017, (the "Report"), I, John R. Beaver, Senior Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (i) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: March 14, 2018

By: /s/ JOHN R. BEAVER

John R. Beaver
Senior Vice President and Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

