

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

FORM 10-K

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

FOR THE YEAR ENDED DECEMBER 31, 1999

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: 001-14429

SKECHERS U.S.A., INC.  
(Exact name of registrant as specified in its charter)

DELAWARE 95-4376145  
(STATE OR OTHER JURISDICTION OF (I.R.S. EMPLOYER  
INCORPORATION OR ORGANIZATION) IDENTIFICATION NO.)  
228 MANHATTAN BEACH BLVD.  
MANHATTAN BEACH, CALIFORNIA 90266  
(ADDRESS OF PRINCIPAL EXECUTIVE (ZIP CODE)  
OFFICES)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (310) 318-3100

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of each class -----	Name of each exchange on which registered -----
Class A Common Stock \$0.001 par value	New York Stock Exchange

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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 the Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the voting stock held by non-affiliates of the registrant based upon the closing sales price of its Class A Common Stock on March 28, 2000 on the New York Stock Exchange was approximately \$100.1 million.

The number of shares of Class A Common Stock outstanding as of March 28, 2000 was 8,481,623.

The number of shares of Class B Common Stock outstanding as of March 28, 2000 was 26,423,445.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement issued in connection with the 2000 Annual Meeting of the Stockholders of the Registrant are incorporated by reference into Part III.

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SKECHERS U.S.A., INC.

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1999

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PART I

ITEM 1. BUSINESS

Certain information contained in this report constitutes forward-looking statements which involve risks and uncertainties including, but not limited to, information with regard to the Company's plans to increase the number of retail locations, and styles of footwear, the maintenance of customer accounts and expansion of business with such accounts, the successful implementation of the Company's strategies, future growth and growth rates and future increases in net sales, expenses, capital expenditures and net earnings. The words "believes," "anticipates," "plans," "expects," "may," "will," "intends," "estimates," and similar expressions are intended to identify forward-looking statements. These forward-looking statements involve risks and uncertainties, and the Company's actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those set forth under "Risk Factors" and elsewhere in this Report.

GENERAL

Skechers U.S.A., Inc. (the "Company" or "Skechers") designs and markets branded contemporary casual, active, rugged and lifestyle footwear for men, women and children. The Company's objective is to become a leading source of contemporary casual and active footwear while ensuring the longevity of both the Company and the Skechers brand name through controlled, well managed growth. The Company strives to achieve this objective by developing and offering a balanced assortment of basic and fashionable merchandise across a wide spectrum of product categories and styles, while maintaining a diversified, low-cost sourcing base and controlling the growth of its distribution channels. The Company sells its products to department stores such as Nordstrom, Macy's, Dillard's, Robinsons-May, and JC Penney and specialty retailers such as Footlocker, Famous Footwear, Genesco's Journeys and Jarman chains, and Footaction U.S.A. The Company also sells its products internationally in over 100 countries and territories through major international distributors.

The Company's product offerings of men's, women's and children's footwear appeal to a broad customer base between the ages of 5 and 40 years. The Company's strategy of providing a growing and balanced assortment of quality basic footwear and seasonal and fashion footwear with progressive styling at competitive prices gives Skechers this broader based customer appeal. Skechers men's and women's footwear are primarily designed with the active, youthful lifestyle of the 12 to 25 year old age group in mind. The Company's product offerings include casual and utility oxfords, loggers, boots and demi-boots; skate, street and fashion sneakers; hikers, trail runners and joggers; sandals,

slides and other open-toe footwear; and dress casual shoes. The Company continually seeks to increase the number of styles offered and the breadth of categories with which the Skechers brand name is identified.

The Company's management and design team collectively possess extensive experience in the footwear industry. Robert Greenberg and Michael Greenberg, the Chairman of the Board and President, respectively, founded the Company in 1992. Prior to that time, Robert Greenberg had co-founded L.A. Gear, Inc. ("L.A. Gear")

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and, together with a management team which included Michael Greenberg, was instrumental in L.A. Gear's growth until his resignation in early 1992. The Greenbergs are joined on the management team by several design, merchandise, production, and marketing executives with experience in a broad range of industries. Management believes this core group comprises an effective and efficient management and design team with the experience to recognize and respond to emerging consumer trends and demands.

#### FOOTWEAR

Skechers offers men's, women's and children's footwear in a broad range of styles, fabrics and colors. The Company offers a broad selection of merchandise in an effort to maximize its ability to respond to changing fashion trends and consumer preferences as well as to limit its exposure to any specific style. The Company believes that its products and brand offer a broad appeal to men, women and children.

The Company introduced its first footwear line with the Skechers brand name in December 1992. Since that time, the Company has expanded its product offerings and grown its net sales while substantially increasing the breadth and penetration of its account base. The Company currently categorizes its footwear in three major product lines: (i) USA (men's and women's), (ii) Sport, and (iii) Skechers Collection. These general product lines are offered in varying styles for men, women and children (except for Skechers Collection which is currently offered in men's styles only).

Skechers USA. The Company's Skechers USA category (also referred to as the "Lifestyle" products) includes four types of footwear: (i) Sport Utility, (ii) Utility, (iii) Classics, and (iv) Hikers. The Sport Utility category includes generally "Black & Brown" boots and shoes that have a rugged, less refined design with industrial-inspired fashion features. This category is defined by the heavy-lugged outsole and value-oriented materials employed in the uppers. Uppers are typically constructed of oiled suede and "Crazy Horse" or distressed leathers which enhance the rugged appearance of the boots and oxfords of this category. The Company designs and prices this category to appeal primarily to young men with broad acceptance across age groups. Suggested retail price points range from \$45.00 to \$65.00 for this category. The Company's Utility styles consist of a single category of boots that are designed to meet the functional demands of a work boot but are marketed as casual footwear. The outsoles of this category are designed to be durable and wearable with Goodyear welted, hardened rubber outsoles. Uppers are constructed of thicker, better grades of heavily oiled leathers. Utility boots may include steel toes, water-resistant or water-proof construction and/or materials, padded collars and Thermolite insulation. Styles include logger boots and demi-boots, engineer boots, motorcycle boots and six-and eight-eyelet work boots. Suggested retail price points range from \$80.00 to \$100.00 for this category. The Classics styles include comfort oriented design and performance features. Boots and shoes in this category employ softer outsoles which are often constructed of polyvinyl carbon ("PVC"). The more refined design of this footwear employs better grades of leather and linings than those used in the Company's Sport Utility boots and shoes. Uppers are generally constructed of grizzly leather or highly-finished leather that produces a waxy shine. Designs are sportier than the Sport Utility category and feature oxfords, wingtips, monkstraps, demi-boots and boots. Suggested retail price points range from \$70.00 to \$85.00 for this category. The Company's Hiker styles consist of a single category of boots and demi-boots that

include many comfort and technical performance features that distinguish this footwear as Hikers. The Company markets this footwear primarily on the basis of style and comfort rather than on technical performance. However, many of the technical performance features in the Hikers contribute to the level of comfort this footwear provides. Outsoles generally consist of molded and contoured hardened rubber. Many designs may include gusseted tongues to prevent penetration of water and debris, cushioned mid-soles, motion control devices such as heel cups, water-resistant or water-proof construction and materials and heavier, more durable hardware such as metal D-rings instead of eyelets. Uppers are generally constructed of heavily oiled nubuck and full-grain leathers. Suggested retail price points range from \$55.00 to \$100.00 for this category. Skechers Sport. Skechers Sport or "Active Street" footwear include skate sneakers, joggers, trail runners, sport hikers and multi-functional shoes inspired by cross-trainers. The Company distinguishes its Skechers Sport category by its technical performance inspired looks; however, generally the Company does not

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promote the technical performance features of these shoes. Certain of the Company's skate sneakers are designed with the technical performance features necessary for competitive level skateboarding. The skate sneaker styles ("Street Sneaker") are designed to appeal to the teenager whose casual shoe of choice is a skate or street sneaker and is intended to be retailed through specialty casual shoe stores and department stores. The other Skechers Sport footwear styles include comfort performance not available in the Street Sneaker styles. The Skechers Sport designs are light-weight constructions that include cushioned heels, polyurethane mid-soles, phylon and other synthetic outsoles and white leather or synthetic uppers such as durabuck and cordura and ballistic nylon mesh. The Skechers Sport features electric and technically inspired hues in addition to the traditional athletic white. Skechers Sport is marketed through traditional athletic footwear specialty retailers as well as basic existing accounts. Suggested retail price points range from \$40.00 to \$70.00 for this category.

Skechers Collection. The Skechers Collection, introduced in 1998, features dress casual shoes designed to complement a young man's semi-formal attire. This category features more sophisticated designs influenced, in part, by prevailing trends in Italy and other European countries. As such, this footwear is more likely than other categories to be sourced from Italy and Portugal. Outsoles project a sleeker profile, while uppers are constructed of glossy, "box" leather and aniline, resulting in a highly polished appearance. Designs include monkstraps, wingtips, oxfords, cap toes and demi-boots and often feature blind-eyelets to enhance the sophisticated nature of the styling. Suggested retail price points range from \$85.00 to \$130.00 for this category.

The Company offers sandalized footwear which features open-toe and open-side constructions consistent with the Company's offering in the Skechers USA, Skechers Sport and Skechers Collection categories of footwear. Such footwear includes fisherman's sandals, shower sandals, beach sandals, slides, comfort-oriented land sandals and technically-inspired water sport sandals. Sandalized footwear includes both leather and synthetic constructions and may feature suede footbeds with form-fitting mid-soles. The Company typically delivers its sandalized footwear to retailers from February to August. Suggested retail price points range from \$20.00 to \$60.00 for this category.

In early 1996, the Company substantially increased its product offerings and marketing focus on its children's footwear line. The children's line features a range of products including boots, shoes and sneakers. The Skechers children's line is comprised primarily of shoes that are designed like their adult counterparts but in "takedown" versions, so that the younger set can wear the same popular styles as their older siblings and schoolmates. This "takedown" strategy maintains the integrity of the product in the premium leathers, hardware and outsoles without the attendant costs involved in designing and developing new products. In addition, the Company also adapts current fashion from the Company's men's and women's lines by modifying designs and choosing colors and materials that are more suitable to the playful image Skechers has

established in the children's footwear market. In 1999, the Company launched its Skechers Lights category, which is a line of lighted footwear combining sequencing patterns and lights in the outsole and other areas of the shoes. Skechers' children's footwear is currently offered at domestic retail prices ranging from \$20.00 to \$50.00.

#### PRODUCT DESIGN AND DEVELOPMENT

Management believes that its product success is related in large part to its ability to recognize trends in the footwear markets and to design products which anticipate and accommodate consumers' ever-evolving preferences. The Company strives to analyze, interpret and translate current and emerging lifestyle trends. Lifestyle trend information is compiled by Skechers' designers through various methods designed to monitor changes in culture and society, including (i) review and analysis of modern music, television, cinema, clothing, alternative sports and other trend-setting media, (ii) travel to domestic and international fashion markets to identify and confirm current trends, (iii) consultation with the Company's retail customers for information on current retail selling trends, (iv) participation in major footwear trade shows to stay abreast of popular brands, fashions and styles and (v) subscription to various fashion and color

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information services. In addition, a key component of Skechers' design philosophy is to continually reinterpret both its basic and current successful styles in the Skechers image.

The Company intends to continue to leverage its reputation for quality products and its relationships with retailers through, among other things, the introduction of new styles in its existing and also new categories of footwear. Also, the Company believes it enhances its position with retailers through its in-stock inventory program. This program increases the availability of Skechers' best-selling products, which management believes has contributed to more consistent product flow to its retail customers and an increased ability to respond to reorder demand.

Offer a Breadth of Innovative Products. The Company has continued to broaden its product line in an effort to reach a larger consumer base. In addition, offering broader products allows the Company to increase sales to its current customer and consumer base. The Company offers a wide variety of different styles of footwear generally in three to four different colors and material variations typically in 10 to 12 different sizes. These styles span a broad spectrum of product categories ranging from skate and street sneakers to fashion sneakers, from steel toe boots with heavy-lugged soles to casual dress shoes for men. The Company has developed this breadth of merchandise offerings in an effort to improve its ability to respond to changing fashion trends and customer preferences, as well as to limit its exposure to any single industry participant. Management does not believe that any single industry participant competes directly with the Company across its entire product offering. Although major new product introductions take place in advance of both the spring and the fall selling seasons, the Company typically introduces new designs in its existing lines every 30 to 60 days to keep current with emerging trends.

Design Team. All of the Company's footwear is designed with an active, youthful lifestyle in mind. The design team's primary mandate is to design shoes marketable to the 12 to 25 year old consumer. While these designs are contemporary in styling, management believes that substantially all of the line appeals to the broader 5 to 40 year old consumer. Although many of the Company's shoes have performance features, such as hikers, trail runners, skate sneakers and joggers, the Company generally does not position its shoes in the marketplace as technical performance shoes. The Company's principal goal in product design is to generate new and exciting footwear with contemporary and progressive style features and comfort enhancing performance features. Management does not believe that technology is a differentiating factor in

marketing footwear in the casual shoe industry.

The footwear design process typically begins about nine months before the start of a season. Skechers' products are designed and developed by the Company's in-house staff. The Company also utilizes outside design firms on an item-specific basis to supplement its design efforts. Separate design teams focus on each of the men's, women's and children's categories, reporting to the Company's Vice President of Design, who has over nine years of experience in footwear design. The design process is extremely collaborative; members of the design staff meet weekly with the heads of retail and merchandising, sales, production and sourcing to further refine the Company's products in order to meet the particular needs of the Company's markets.

After the design team arrives at a consensus regarding the fashion themes for the coming season, the group then translates these themes into Skechers products. These interpretations include variations in product color, material structure and decoration, which are arrived at after close consultation with the Company's production department. Prototype blueprints and specifications are created and forwarded to the Company's prototype manufacturers located in Taiwan, which then forward design prototypes back to the Company's domestic design team. New design concepts are often also reviewed by the Company's major retail customers. This customer input not only allows the Company to measure consumer reaction to the latest designs, but also affords the Company an opportunity to foster deeper and more collaborative relationships with its customers. The Company's design team can easily and quickly modify and refine a design based on this development input.

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#### SOURCING

Substantially all of the Company's products are produced in China. The Company does not own or operate any manufacturing facilities. Management believes the use of independent manufacturers increases its production flexibility and capacity while at the same time substantially reducing capital expenditures and avoiding the cost of managing a large production work force. While the Company has long standing relationships with many of its manufacturers and believes its relationships to be good, there are no long-term contracts between the Company and any of its manufacturers.

The Company maintains an in-stock position for selected styles of footwear in order to minimize the time necessary to fill customer orders. In order to maintain an in-stock position, the Company places orders for selected footwear with its manufacturers prior to the time the Company receives customers' orders for such footwear. In order to reduce the risk of overstocking, the Company seeks to assess demand for its products by soliciting input from its customers and monitoring retail sell-through. In addition, the Company analyzes historical and current sales and market data to develop internal product quantity forecasts which helps reduce inventory risks.

Asian Office. To safeguard product quality and consistency, the Company oversees the key aspects of the production process from prototyping through production to finished product. Monitoring is performed by the Company's in-house production department and out of the Company's office in Taiwan. Management believes the Company's Asian presence allows Skechers to negotiate supplier and manufacturer arrangements more effectively and ensure timely delivery of finished footwear. In addition, the Company requires its manufacturers to certify that neither convict, forced, indentured labor (as defined under U.S. law) nor child labor (as defined by the manufacturer's country) was used in the production process, that compensation will be paid according to local law and that the factory is in compliance with local safety regulations.

Factories. Manufacturers are selected in large part on the basis of the Company's prior experience with the manufacturer and the amount of available

production capacity. The Company attempts to monitor its selection of independent factories to ensure that no one manufacturer is responsible for a disproportionate amount of the Company's merchandise. In addition, the Company seeks to use, whenever possible, manufacturers that have previously produced the Company's footwear, which the Company believes enhances continuity and quality while controlling production costs. The Company generally limits product orders to 30.0% or less of that manufacturer's total production at any one period of time. In addition, the Company sources product for styles that account for a significant percentage of the Company's net sales from at least three different manufacturers. For the year ended December 31, 1999, the Company had four manufacturers which accounted for 15.5%, 13.4%, 13.3% and 12.3% of total purchases, respectively.

Quality Control. Management believes that quality control is an important and effective means of maintaining the quality and reputation of its products. The Company's quality control program is designed to ensure that finished goods not only meet with Company established design specifications, but also that all goods bearing its trademarks meet the Company's standards for quality. Quality control personnel perform an array of inspection procedures at various stages of the production process, including examination and testing of (i) prototypes of key products prior to manufacture, (ii) samples and materials prior to production and (iii) final products prior to shipment. The Company employees are on-site at each of Skechers' major manufacturers to oversee in person key phases of production. In addition, unannounced visits to the manufacturing sites to further monitor compliance with Skechers' manufacturing specifications are made by the Company employees and agents.

#### MARKETING AND PROMOTION

The Company's marketing focus is to maintain and enhance recognition of the Skechers brand name as a casual, active youthful brand that stands for quality, comfort and design innovation. Senior management is directly involved in shaping the Company's image and its advertising and promotional activities. Towards this end, the Company endeavors to spend between 8.0% and 10% of annual net sales in the marketing of Skechers footwear through an integrated effort of advertising, promotions, public relations, trade shows and other marketing efforts, which the Company believes substantially heightens brand awareness.

Advertising. Management believes that the Company's success to date is due in large part to its advertising strategies and methods. The Company's in-house marketing and advertising team has developed a comprehensive program to promote the Skechers brand name through lifestyle and image advertising. The Company has made a conscious effort to avoid the association of the Skechers name with any single category of shoe to provide merchandise flexibility and to aid the ability to take the brand and product design in the direction of evolving footwear fashions and consumer preferences. The Company uses a variety of media for its national advertising. Print efforts are represented by one or two page collage features in popular fashion and lifestyle consumer publications that appeal to the Company's target customer group. Skechers' progressive television advertisements are primarily created in-house and air frequently on top television shows. Different advertisements are created for each of the 5 to 9, 10 to 24 and 25 to 35 year old consumer groups.

Certain of the Company's retail accounts feature "in-store shop" formats in which the Company provides fixtures, signage and visual merchandise assistance in a dedicated floor space within the store. The design of the shops utilizes the distinctive Skechers advertising strategies to promote brand recognition and differentiate Skechers' presence in the store from that of its competition. The installation of these "in-store shops" enables the Company to establish premium locations within the retailers and management believes it aids in increased sell-through and higher maintained margins for the Company's customers. The Company's in-house display merchandising department supports retailers and



distributors by developing point-of-purchase advertising to further promote its products in stores and to leverage the brand recognition at the retail level.

Promotions. Skechers' in-house promotions department is responsible for building national brand name recognition. Teaming up with national retailers and radio stations, the promotions department is responsible for cross promotions, which help draw customers to retail store locations.

Public Relations. The Company's in-house public relations department is responsible for increasing Skechers' media exposure. The department communicates the Skechers image to the public and news media through the active solicitation of fashion editorial space, arranging interviews with key Company personnel and coordinating local publicity and special events programs for the Company, including celebrity appearances and fashion shows. With its strategy tied to promoting the newest styles produced by the product development team, Skechers' products are often featured in fashion and pop culture magazines and on a select group of films and popular television shows. For example, Skechers shoes have been prominently displayed on the television series Dharma & Greg and referenced in the film 10 Things I Hate About You.

Trade Shows. To showcase the Skechers product to footwear buyers, in 1999, the Company exhibited at 13 trade shows. The Company prides itself on having innovative and dynamic exhibits on the show floor. Designed in-house, the Company's state-of-the-art trade show exhibits feature the latest products and provide a stage for Skechers' internally developed music-video-style dance and stage shows featuring progressive music and nightclub lighting.

Electronic Commerce and Mail-Order Catalog. In 1998, the Company launched its initial product mail order catalog. Concurrently, Skechers went live with its interactive website ([www.skechers.com](http://www.skechers.com)). It features the Company's current mail-order catalog for on-line shopping. It also features photos, interviews and information on Company-sponsored events. The Company's website and mail-order catalog are intended to further enhance the Skechers brand image.

#### DISTRIBUTION CHANNELS

Skechers has implemented a strategy of controlling the growth of the distribution channels through which the Company's products are sold in order to protect the Skechers brand name, properly service customer accounts and better manage the growth of the business. The Company has limited distribution of its product to those retailers which management believes can best support the Skechers brand name in the market. By focusing on the Company's existing accounts, the Company can deepen its relationships with its existing customers by providing a heightened level of customer service. Management believes close relationships with its customers help the Company to maximize their customers' (i) retail sell-through, (ii) maintained margins and (iii) inventory turns. Limiting product distribution to the appropriate accounts and closely working with those accounts also helps the Company to reduce its own inventory markdowns and customer returns and allowances while maintaining the proper showcase for the Skechers brand name and product.

Sales and Field Service Representatives. As of February 29, 2000, the Company has 86 and 8 sales and field service representatives, respectively. Each of the sales representatives is compensated on a salary plus commission basis; the representatives sell Skechers products exclusively. Senior management, specifically Michael Greenberg, is actively involved in selling to and maintaining relationships with Skechers' major retail accounts. For the year ended December 31, 1999 the top five sales persons accounted for 43.7% of the Company's net domestic sales. One of these salespersons generated 14.5% of the Company's net domestic sales for the year ended December 31, 1999.

The field service representatives ensure proper presentation of Skechers' merchandise and point-of-purchase marketing materials. The Company's sales and field service personnel work closely with the accounts to coordinate the

appropriate inventory level and product mix that should be carried in each store in an effort to help retail sell-through and enhance the customer's product margin. Such information is then used as a basis for developing sales projections and product needs for such customers. This information in turn assists the Company with scheduling production. Along with a staff of in-house customer service employees, the Company is committed to achieving customer satisfaction and to building a loyal customer base by providing a high level of knowledgeable, attentive and personalized customer service.

Concept Stores. As of December 31, 1999, the Company operated 23 concept stores at marquee locations in major metropolitan cities. The stores are typically designed to create a distinctive Skechers look and feel and enhance customer association of the Skechers brand with current youthful lifestyle trends and styles. The concept stores feature modern music and lighting and present an open floor design to allow customers to readily view the merchandise on display. These concept stores serve a threefold purpose in the Company's operating strategy. First, concept stores serve as a showcase for the full range of the Company's product offerings for the current season, providing the customer with the entire product story. In contrast, management estimates that its average retail customer carries no more than 5.0% of the complete Skechers line. Second, retail locations are generally chosen to generate maximum marketing value for the Skechers brand name through signage and store front presentation. Third, the Company's concept stores also serve as marketing and product testing venues by providing rapid product feedback. Management believes that product sell-through information derived from the Company's concept stores enables the Company's sales, merchandising and production staff to respond quickly to market changes and new product introductions. The Company occasionally orders limited production runs which may initially be tested in Skechers' concept stores. By working closely with store personnel, the Company obtains customer feedback that often influences product design and development. Management believes that sales in Skechers' retail stores can help forecast sales in national retail stores. Such responses serve to augment sales and limit the Company's inventory markdowns and customer returns and allowances. Management adjusts its product and sales strategy based upon seven to 14 days of retail sales information.

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The Company seeks to instill enthusiasm and dedication in its concept store management personnel and sales associates through incentive programs and regular communication with store personnel. Sales associates receive commissions on sales with a guaranteed minimum compensation. Concept store managers receive base compensation plus incentive compensation based on sales. The Company has well-established concept store operating policies and procedures and utilizes an in-store training regimen for all new store employees. Merchandise presentation instructions and detailed product descriptions also are provided to sales associates to enable them to gain familiarity with Skechers product offerings.

Factory and Warehouse Outlet Stores. As of December 31, 1999, the Company also operated 19 factory and warehouse outlet stores that enable the Company to liquidate excess, discontinued and odd-size inventory in a cost-efficient manner. Inventory in these stores is supplemented by certain first-line styles sold at full retail price points. The factory outlet stores are generally located in manufacturers' outlet centers throughout the country. The Company's factory outlet stores have enabled it to increase sales in certain geographic markets where Skechers' products were not previously available and to consumers who favor value-oriented retailers. The outlets provide opportunities for the Company to sell discontinued and excess merchandise, thereby reducing the need to sell such merchandise to discounters at excessively low prices. The Company's free-standing warehouse outlet stores enable it to liquidate other excess merchandise, discontinued lines and odd sizes. The Company strives to geographically position its factory and warehouse outlet stores to minimize potential conflicts with the Company's retail customers.

Other Direct Distribution Outlets. The Company's mail-order catalog and website act as sales vehicles. Management believes that these distribution channels will not generate material growth for the Company in the near term; however, management believes that they may present attractive long-term opportunities with minimal near-term costs.

#### INTERNATIONAL OPERATIONS

Although the Company's primary focus is on the domestic market, the Company presently markets its product in countries and territories in Europe, Asia and selected other foreign regions. Skechers derives revenues and earnings from outside the United States from two principal sources: (i) sales of Skechers footwear directly to foreign distributors who distribute such footwear to department stores and specialty retail stores and (ii) to a lesser extent, royalties from licensees who manufacture and distribute Skechers products outside the United States.

Management believes that international distribution of Skechers products may represent a significant opportunity to increase revenue and profits. Although the Company is in the early stages of its international expansion, Skechers products are currently sold in more than 100 countries and territories. The Company's goal is to increase international sales through foreign distributors by heightening the Company's international marketing presence in those countries. In 1998, the Company launched its first major international advertising campaign, which was designed to establish Skechers as a global brand synonymous with casual shoes. This advertising campaign continued during 1999. The Company is exploring selling directly to retailers in certain European countries in the near future. In addition, the Company is exploring selectively opening flagship retail stores internationally on its own or through joint ventures.

#### DISTRIBUTION FACILITY

The Company believes that strong distribution support is a critical factor in the Company's operations. Following the manufacturing, the Company's products are packaged in shoe boxes bearing bar codes and generally either shipped to the Company's approximately 700,000 square feet of leased distribution centers located in Ontario, California, or shipped directly from the manufacturer to Skechers' international customers. Upon receipt at the central distribution centers, merchandise is inspected and recorded in the

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Company's management information system and packaged according to customers' orders for delivery. Merchandise is shipped to the customer by whatever means the customer requests, which is usually by common carrier. The central distribution centers have multi-access docks, enabling the Company to receive and ship simultaneously and to pack separate trailers for shipments to different customers at the same time. The Company has an electronic data interchange system to which some of the Company's larger customers are linked. This system allows these customers to automatically place orders with the Company, thereby eliminating the time involved in transmitting and inputting orders, and includes direct billing and shipping information.

#### POTENTIAL LICENSING ARRANGEMENTS

Management believes that selective licensing of the Skechers brand name to non-footwear-related manufacturers may broaden and enhance the Skechers image without requiring significant capital investments or additional incremental operating expenses by the Company. From time to time, the Company has experimented with certain manufacturers on a very limited basis to study the potential impact of licensing the brand. The Company currently has licensing agreements internationally for apparel with Life Gear Corporation in Japan and for footwear with Pentland Group PLC in the United Kingdom. Management believes

that revenues from licensing agreements will not be a material source of growth for the Company in the near term; however, management believes that licensing arrangements may present attractive long-term opportunities with minimal near-term costs.

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#### BACKLOG

The Company generally receives the bulk of the orders for each of the spring and fall seasons a minimum of three months prior to the date the products are shipped to customers. At December 31, 1999, the Company's backlog was \$121.7 million, compared to \$74.9 million at December 31, 1998. To manage inventory risk, the Company estimates its production requirements and engages in certain other inventory management techniques. For a variety of reasons, including the timing of shipments, product mix of customer orders and the amount of in-season orders, backlog may not be a reliable measure of future sales for any succeeding period.

#### INTELLECTUAL PROPERTY RIGHTS

The Company owns and utilizes a variety of trademarks, including the Skechers trademark. As of December 31, 1999, the Company had approximately 30 registrations and approximately 60 pending applications for its trademarks in the United States. In addition, as of December 31, 1999, the Company had approximately 431 trademark registrations and applications in approximately 80 foreign countries. The Company also had 45 design patents issued and approximately 26 design patent applications pending in the United States. The Company regards its trademarks and other intellectual property as valuable assets and believes that they have significant value in the marketing of its products. The Company vigorously protects its trademarks against infringement, including through the use of cease and desist letters, administrative proceedings and lawsuits.

The Company relies on trademark, patent, copyright and trade secret protection, and, non-disclosure agreements and licensing arrangements to establish, protect and enforce intellectual property rights in the design of its products. In particular, the Company believes that its future success will depend in significant part on the Company's ability to maintain and protect the Skechers trademark. Despite the Company's efforts to safeguard and maintain its intellectual property rights, there can be no assurance that the Company will be successful in this regard. There can be no assurance that third parties will not assert intellectual property claims against the Company in the future. Furthermore, there can be no assurance that the Company's trademarks, products and promotional materials or other intellectual property rights do not or will not violate the intellectual property rights of others, that its intellectual property would be upheld if challenged, or that the Company would, in such an event, not be prevented from using its trademarks or other intellectual property rights. Such claims, if proved, could materially and adversely affect the Company's business, financial condition and results of operations. In addition, although any such claims may ultimately prove to be without merit, the necessary management attention to and legal costs associated with litigation or other resolution of future claims concerning trademarks and other intellectual property rights could materially and adversely affect the Company's business, financial condition and results of operations. The Company has sued and has been sued by third parties for infringement of intellectual property. It is the opinion of management that none of these claims have materially impaired the

Company's ability to utilize its trademarks.

The laws of certain foreign countries do not protect intellectual property rights to the same extent or in the same manner as do the laws of the United States. Although the Company continues to implement protective measures and intends to defend its intellectual property rights vigorously, there can be no assurance that these efforts will be successful or that the costs associated with protecting its rights in certain jurisdictions will not be prohibitive.

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From time to time, the Company discovers products in the marketplace that are counterfeit reproductions of the Company's products or that otherwise infringe upon intellectual property rights held by the Company. There can be no assurance that actions taken by the Company to establish and protect its trademarks and other intellectual property rights will be adequate to prevent imitation of its products by others or to prevent others from seeking to block sales of the Company's products as violating trademarks and intellectual property rights. If the Company is unsuccessful in challenging a third party's products on the basis of infringement of its intellectual property rights, continued sales of such product by that or any other third party could adversely impact the Skechers brand, result in the shift of consumer preferences away from the Company and generally have a material adverse effect on the Company's business, financial condition and results of operations.

#### COMPETITION

Competition in the footwear industry is intense. Although the Company believes that it does not compete directly with any single company with respect to its entire range of products, the Company's products compete with other branded products within their product category as well as with private label products sold by retailers, including some of the Company's customers. The Company's utility footwear and casual shoes compete with footwear offered by companies such as The Timberland Company, Dr. Martens, Kenneth Cole Productions, Steven Madden, Ltd. and Wolverine World Wide, Inc. The Company's athletic shoes compete with brands of athletic footwear offered by companies such as Nike, Inc., Reebok International Ltd., Adidas-Salomon AG and New Balance. The Company's children's shoes compete with brands of children's footwear offered by companies such as The Stride Rite Corporation. In varying degrees, depending on the product category involved, the Company competes on the basis of style, price, quality, comfort and brand name prestige and recognition, among other considerations. These and other competitors pose challenges to the Company's market share in its major domestic markets and may make it more difficult to establish the Company in Europe, Asia and other international regions. The Company also competes with numerous manufacturers, importers and distributors of footwear for the limited shelf space available for the display of such products to the consumer. Moreover, the general availability of contract manufacturing capacity allows ease of access by new market entrants. Many of the Company's competitors are larger, have achieved greater recognition for their brand names, have captured greater market share and/or have substantially greater financial, distribution, marketing and other resources than the Company. There can be no assurance that the Company will be able to compete successfully against present or future competitors or that competitive pressures faced by the Company will not have a material adverse effect on the Company's business, financial condition and results of operations.

#### EMPLOYEES

As of February 29, 2000, the Company employed 888 persons, 549 of which were employed on a full-time basis and 339 of which were employed on a part-time basis. None of the Company's employees are subject to a collective bargaining agreement. The Company believes that its relations with its employees are satisfactory. The Company offers its employees a discount on Skechers merchandise to encourage enthusiasm for the product and Company loyalty.

## RISK FACTORS

In addition to the other information in this Form 10-K, the following factors should be considered in evaluating the Company and its business.

### CHANGING CONSUMER DEMANDS AND FASHION TRENDS

The footwear industry is subject to rapidly changing consumer demands and fashion trends. The Company believes that its success depends in large part upon its ability to identify and interpret fashion trends and to anticipate and respond to such trends in a timely manner. There can be no assurance that the Company will be able to continue to meet changing consumer demands or to develop successful styles in the future. Decisions with respect to product designs often need to be made several months in advance of the time when consumer acceptance can be determined. As a result, the Company's failure to anticipate, identify or react appropriately to changes in styles and features could lead to, among other things, lower sales, excess inventories, higher inventory markdowns, impairment of the Company's brand image and lower gross margins as a percentage of net sales ("Gross Margins") as a result of allowances and discounts provided to retailers. Conversely, the failure by the Company to anticipate consumer demand could result in inventory shortages, which in turn could adversely affect the timing of shipments to customers, negatively impacting retailer and distributor relationships, and diminish brand loyalty. In addition, even if the Company reacts appropriately to changes in consumer preferences, consumers may identify the Company's brand image with an outmoded fashion or the association of the brand may be limited to styles or categories of footwear no longer in demand. There can

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be no assurance that the Company will successfully adapt to changing consumer demands and fashion trends, and any such failure to adapt could have a material adverse effect on the Company's business, financial condition and results of operations. Because of these risks, a number of companies in the footwear industry, and in the fashion and apparel industry, have experienced periods, which can be over several years, of rapid growth in revenues and earnings and thereafter periods of declining sales and losses which in some cases have resulted in the companies ceasing to do business. Until January 1992, several of the Company's executive officers and key employees were employed by L.A. Gear, Inc., an athletic and casual footwear and apparel company, which experienced similar fluctuations.

The Company intends to market additional lines of footwear in the future and, as is typical with new products, demand and market acceptance will be subject to uncertainty. Failure to regularly develop and introduce new products successfully could materially and adversely impact the Company's future growth and profitability. Achieving market acceptance for new products may require substantial marketing efforts. There can be no assurance that the Company's marketing efforts will be successful or that the Company will have the funds necessary to undertake sufficient efforts.

### RISKS RELATING TO STYLE CONCENTRATION

If any one style or group of similar styles of the Company's footwear were to represent a substantial portion of the Company's net sales, the Company could be exposed to risk should consumer demand for such style or group of styles decrease in subsequent periods. In the past, gross sales were adversely affected by decreased consumer demand for a style of footwear that previously represented a significant portion of the Company's sales. This style no longer represents a significant portion of the Company's sales. The Company attempts to hedge this risk by offering a broad range of products, and no style comprised over 5.0% of the Company's gross wholesale sales, net of discounts, for the year ended December 31, 1999. There can be no assurance that fluctuations in sales of any given style that represents a significant portion of the Company's net sales will not recur in the future and have a material adverse effect on the Company's business, financial condition and results of operations.

#### ABILITY TO MANAGE GROWTH

The Company has experienced rapid growth over the past three years and remains vulnerable to a variety of business risks generally associated with rapidly growing companies. The Company intends to continue to pursue an aggressive growth strategy through expanded marketing and promotion efforts, frequent introductions of products, broader lines of casual and performance footwear, expansion of retail stores and increased international market penetration, all of which may place a significant strain on the Company's financial, management and other resources. The Company's future performance will depend in part on its ability to manage change in both its domestic and international operations and will require the Company to attract, train, manage and retain management, sales, marketing and other key personnel. The Company's ability to manage its growth effectively will require it to continue to improve its operational and financial control systems, infrastructure and management information systems. For example, in early 1998, the Company moved its distribution center to a larger facility and currently intends to install a new material handling system at its second distribution facility in latter part of 2000 at a total cost of approximately \$12.0 million. There can be no assurance that these expansion efforts will be successfully completed or that they will not interfere with existing operations. The inability of the Company's management to manage growth effectively could have a material adverse effect on the Company's business, financial condition and results of operations.

#### ABILITY TO SUSTAIN PRIOR RATE OF GROWTH OR INCREASE NET SALES OR EARNINGS

The Company has realized rapid growth since inception, increasing net sales at a compound annual growth rate of 36.2% from \$90.8 million in 1994 to \$424.6 million in 1999. From 1998 to 1999, the Company experienced a 13.9% and 14.2% increase in net sales and earnings from operations, respectively. In the future, the Company's rate of growth will be dependent upon, among other things, the continued success of

its efforts to expand its footwear offerings and distribution channels. The Company's profitability in any calendar quarter of any fiscal year depends upon, among other things, the timing and level of advertising and trade show expenditures and the timing and level of shipments of seasonal merchandise. There can be no assurance that the Company's rate of growth will not decline or that it will be profitable in any quarter of any succeeding fiscal year. In addition, the Company may have more difficulty maintaining its prior rate of growth to the extent it becomes larger.

As part of its growth strategy, the Company seeks to further penetrate existing retail accounts, open its own retail stores in selected locations and increase its international operations, including distributing in countries and territories where the Company has little distribution experience and where the Company's brand name is not yet well known. There can be no assurance that these and the Company's other growth strategies will be successful. Success will depend on various factors, including the strength of the Company's brand name, market success of current and new products, competitive conditions, the ability of the Company to manage increased net sales and stores and the availability of desirable locations. The Company's business also depends on general economic conditions and levels of consumer spending, which are currently high, and a decline in the economy or a recession could adversely impact the Company's business, financial condition and operating results since consumers often reduce spending on footwear and apparel in such times. There can be no assurance that the Company will be able to increase its sales to existing customers, open and operate new retail stores or increase its international operations on a profitable basis or that the Company's earnings from operations as a percentage of net sales ("Operating Margins") will improve, and there can be no assurance that the Company's growth strategies will be successful or that the Company's

net sales or net earnings will increase as a result of the implementation of such strategies. In addition, the Company has significantly expanded its infrastructure and personnel to achieve economies of scale in anticipation of continued increases in net sales. Because these expenses are fixed, at least in the short term, operating results and margins would be adversely impacted if the Company does not achieve anticipated continued growth.

#### RISKS ASSOCIATED WITH FOREIGN OPERATIONS

Substantially all of the Company's net sales for the year ended December 31, 1999 were derived from sales of footwear manufactured for the Company outside of the United States. During such period, substantially all of such manufactured products were produced in China. Additionally, the Company intends to increase its international sales efforts. Foreign manufacturing and sales are subject to a number of risks, including work stoppages, transportation delays, changing economic conditions, expropriation, international political tension, political and social unrest, nationalization, the imposition of tariffs, import and export controls and other nontariff barriers, exposure to different legal standards (particularly with respect to intellectual property), burdens with complying with a variety of foreign laws and changes in domestic and foreign governmental policies, any of which could have a material adverse effect on the Company's business, financial condition and results of operations. The Company has not experienced material losses as a result of fluctuation in the value of foreign currencies. The Company's net sales and cost of goods sold are denominated in U.S. Dollars; consequently, the Company does not engage in currency hedging. Nevertheless, currency fluctuations could adversely affect the Company in the future. Also, the Company may be subjected to additional duties, significant monetary penalties, the seizure and the forfeiture of the products the Company is attempting to import or the loss of its import privileges if the Company or its suppliers are found to be in violation of U.S. laws and regulations applicable to the importation of the Company's products. Such violations may include (i) inadequate record keeping of its imported products, (ii) misstatements or errors as to the origin, quota category, classification, marketing or valuation of its imported products, (iii) fraudulent visas or (iv) labor violations under U.S. or foreign laws. There can be no assurance that the Company will not incur significant penalties (monetary or otherwise) if the United States Customs Service determines that these laws or regulations have been violated or that the Company failed to exercise reasonable care in its obligations to comply with these laws or regulations on an informed basis. Such factors could render the conduct of business in a particular country undesirable or impractical, which could have a material adverse effect on the Company's business, financial condition and results of operations. The Company continues to monitor the political and economic stability of the Asian countries with which it conducts business. A substantial portion of the Company's footwear is manufactured in China. China has been granted "normal trade relations" status under United States tariff laws through early July 2000, which provides a favorable

category of United States import duties. As a result of continuing concerns in the United States Congress regarding China's human rights policies, disputes regarding Chinese trade policies, including the country's inadequate protection of United States intellectual property rights, and current relations with China regarding weapons information, there has been, and may be in the future, opposition to the extension of "normal trade relations" status for China. In 2000, however, there will be for the first time, a major effort by the U.S. Congress to pass legislation that would make permanent China's "natural trade relations" status in return for the country's expected accession to the World Trade Organization. The proposal is controversial, and there can be no assurance that it will be passed. Moreover, there can be no assurance that China will continue to enjoy "natural trade relations" status in the future. The loss of "normal trade relations" status for China would result in a substantial increase in the import duty of goods manufactured in China and imported into the United



States and would result in increased costs for the Company. Such increases in import duties and costs could have a material adverse effect on the Company's business, financial condition and results of operations.

Although the footwear sold by the Company is not currently subject to quotas in the United States, certain countries in which the Company's products are sold are subject to certain quotas and restrictions on foreign products which to date have not had a material adverse effect on the Company's business, financial condition and results of operations. However, such countries may alter or modify such quotas or restrictions. Countries in which the Company's products are manufactured may, from time to time, impose new or adjust quotas or other restrictions on exported products, and the United States may impose new duties, tariffs and other restrictions on imported products, any of which could have a material adverse effect on the Company's business, financial condition and results of operations and its ability to import products at the Company's current or increased quantity levels. Other restrictions on the importation of the Company's products are periodically considered by the U.S. Congress, and there can be no assurance that tariffs or duties on the Company's products may not be raised, resulting in higher costs to the Company, or that import quotas with respect to such products may not be imposed or made more restrictive.

#### DEPENDENCE ON CONTRACT MANUFACTURERS

The Company's footwear products are currently manufactured by independent contract manufacturers. For the year ended December 31, 1999, the top four manufacturers of the Company's manufactured products accounted for 15.5%, 13.4%, 13.3% and 12.3% of total purchases, respectively. The Company has no long-term contracts with its manufacturers and competes with other footwear companies for production facilities. Although the Company has established close working relationships with its principal manufacturers, the Company's future success will depend, in large part, on maintaining such relationships and developing new relationships. There can be no assurance that the Company will not experience difficulties with such manufacturers, including reduction in the availability of production capacity, failure to meet the Company's quality control standards, failure to meet production deadlines or increase in manufacturing costs. This could result in cancellation of orders, refusal to accept deliveries or a reduction in purchase prices, any of which could have a material adverse effect on the Company's business, financial condition and results of operations. In the event that the Company's current manufacturers were for any reason to cease doing business with the Company, the Company could experience an interruption in the manufacture of its products, which could have a material adverse effect on the Company's business, financial condition and results of operations. Although the Company believes that it could find alternative sources to manufacture its products within 90 to 120 days after the date of disruption, establishment of new manufacturing relationships involves various uncertainties, including payment terms, costs of manufacturing, adequacy of manufacturing capacity, quality control and timeliness of delivery. The Company cannot predict whether it will be able to establish new manufacturing relationships, either in the countries in which it currently does business or in other countries in which it does not currently do business, that will be as favorable as those that now exist. Any significant delay in manufacture of the Company's footwear products or the inability to provide products consistent with the Company's standards, would have a material adverse effect on the Company's business, financial condition and results of operations.

The Company requires its independent contract manufacturers to operate in compliance with applicable laws and regulations. The Company requires its manufacturers to certify that neither convict, forced, indentured labor (as defined under U.S. law) nor child labor (as defined by the manufacturer's country) was used in the production process, that compensation will be paid in accordance with local law and that the factory is in compliance with local safety regulations. Although the Company's operating guidelines promote ethical business practices and the Company's sourcing personnel periodically visit and

monitor the operations of its independent contract manufacturers, the Company does not control these vendors or their labor practices. The violation of labor or other laws by an independent contract manufacturer of the Company, or the divergence of an independent contract manufacturer's labor practices from those generally accepted as ethical in the United States, could result in adverse publicity for the Company and could have a material adverse effect on the Company's business, financial condition and results of operations.

#### DEPENDENCE ON KEY CUSTOMERS AND SALES REPRESENTATIVES

During the year ended December 31, 1999, the Company's net sales to its five largest customers accounted for approximately 30.8% of total net sales. For the year ended December 31, 1999, no one customer accounted for 10.0% or more of net sales. Although the Company has long-term relationships with many of its customers, none of its customers has any contractual obligations to purchase the Company's products. There can be no assurance that the Company will be able to retain its existing major customers. In addition, the retail industry has periodically experienced consolidation, contractions and closings and any future consolidation, contractions or closings may result in loss of customers or uncollectability of accounts receivables of any major customer in excess of amounts insured by the Company. For example, in late 1998, The Venator Group announced the closure of its Kinney and Footquarters shoe stores and, in early 1999, Edison Brothers closed its Wild Pair shoe stores.

As of December 31, 1999, the Company had one customer which accounted for 10.1% of trade accounts receivable. The loss of or significant decrease in sales to any one of the Company's major customers or uncollectability of any accounts receivable of any major customer in excess of amounts insured could have a material adverse effect on its business, financial condition and results of operations.

The Company has entered into employment agreements with each of its salespersons. Although each salesperson has agreed under these agreements to keep certain information of the Company confidential, these salespersons are not subject to non-competition agreements with the Company. The loss of any of such salespersons may result in the disruption of service to such customers serviced by such salespersons, which could have a material adverse effect on the Company's business, financial condition and results of operations.

#### SEASONALITY; QUARTERLY FLUCTUATIONS

Sales of footwear products have historically been somewhat seasonal in nature with the strongest sales generally occurring in the third and fourth quarters. During 1999, the Company aggressively addressed this seasonal fluctuations by introducing new styles that addressed the seasonal demands. As a result, the Company's third and fourth quarter represented 29.2% and 23.6% of net sales in 1999, respectively, compared to 38.4% and 22.0% of net sales in 1998, respectively. The Company's net sales in the fourth quarter of 1998 were also adversely affected by the overall weakness in the retail footwear market. In the third and fourth quarters of 1999, income from operations represented 39.9% and 15.6% of earnings from operations for the year, as compared to income from operations during the third quarter of 72.0% and a loss from operations was generated in the fourth quarter of 1998. Operating expenses for the fourth quarter of 1998 were impacted by certain discretionary expenses of approximately \$3.2 million and by significantly higher marketing expenses as a percentage of net sales than the Company typically incurs. The Company has experienced and expects to continue to experience some variability in its net sales, operating results and net earnings on a quarterly basis. The Company's domestic customers generally assume responsibility for scheduling pickup and delivery of purchased products. Any delay in scheduling or pickup which is beyond the Company's control, could materially negatively impact the Company's net sales and results of operations for any given quarter. The Company believes the factors which influence this variability include

(i) the timing of the Company's introduction of new footwear products, (ii) the level of consumer acceptance of new and existing products, (iii) general economic and industry conditions that affect consumer spending and retail purchasing, (iv) the timing of the placement, cancellation or pickup of customer orders, (v) increases in the number of employees and overhead to support growth, (vi) the timing of expenditures in anticipation of increased sales and customer delivery requirements, (vii) the number and timing of new Company retail store openings and (viii) actions by competitors. Due to these and other factors, the results for any particular quarter are not necessarily indicative of results for the full year. This cyclically and any related fluctuation in consumer demand could have a material adverse effect on the Company's business, financial condition and results of operations.

#### EXPOSURE TO FLUCTUATIONS IN ECONOMIC CONDITIONS

The footwear industry in general is dependent on the economic environment and levels of consumer spending which affect not only the ultimate consumer, but also retailers, the Company's primary direct customers. Purchases of footwear tend to decline in periods of recession or uncertainty regarding future economic prospects, when consumer spending, particularly on discretionary items, declines. As a result, the Company's operating results may be adversely affected by downward trends in the economy or the occurrence of events that adversely affect the economy in general.

#### RISKS RELATING TO ADVANCE PURCHASES OF PRODUCTS

To minimize purchasing costs, the time necessary to fill customer orders and the risk of non-delivery, the Company places orders for certain of its products with its manufacturers prior to the time the Company has received all of its customers' orders and maintains an inventory of certain products that it anticipates will be in greater demand. There can be no assurance, however, that the Company will be able to sell the products it has ordered from manufacturers or that it has in its inventory. Inventory levels in excess of customer demand may result in inventory write-downs and the sale of excess inventory at discounted prices could significantly impair the Company's brand image and could have a material adverse effect on the Company's business, financial condition and results of operations. As of December 31, 1999, the Company had

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approximately \$98.0 million of open purchase orders with its manufacturers and \$69.0 million of inventory relating to order backlog of \$121.7 million.

#### ADDITIONAL CAPITAL REQUIREMENTS

The Company expects that anticipated cash flow from operations, available borrowings under the Company's revolving line of credit, cash on hand and its financing arrangements will be sufficient to provide the Company with the liquidity necessary to fund its anticipated working capital and capital requirements through 2000. However, in connection with its growth strategy, the Company will incur significant working capital requirements and capital expenditures. The Company's future capital requirements will depend on many factors, including, but not limited to, the levels at which the Company maintains inventory, the market acceptance of the Company's footwear, the levels of promotion and advertising required to promote its footwear, the extent to which the Company invests in new product design and improvements to its existing product design and the number and timing of new store openings. To the extent that available funds are insufficient to fund the Company's future activities, the Company may need to raise additional funds through public or private financing. No assurance can be given that additional financing will be available or that, if available, it can be obtained on terms favorable to the Company. Failure to obtain such financing could delay or prevent the Company's planned expansion, which could adversely affect the Company's business, financial condition and results of operations. In addition, if additional capital is raised through the sale of additional equity or convertible securities, dilution

to the Company's stockholders could occur.

#### DEPENDENCE ON KEY PERSONNEL

The Company's success depends to a large extent upon the expertise and continuing contributions of Robert Greenberg, Chairman of the Board and Chief Executive Officer, Michael Greenberg, President, and David Weinberg, Executive Vice President and Chief Financial Officer. Each of these officers currently has a three-year employment contract with the Company. These agreements do not have non-competition provisions upon termination of employment. The loss of the services of any of these individuals or any other key employee could have a material adverse effect on the Company's business, financial condition and results of operations. The Company's future success also depends on its ability to identify, attract and retain additional qualified personnel. The competition for such employees is intense, and there can be no assurance that the Company will be successful in identifying, attracting and retaining such personnel. The Company maintains \$5.0 million of "key man" life insurance on the life of Robert Greenberg. The loss of key employees or the inability to hire or retain qualified personnel in the future could have a material adverse effect on the Company's business, financial condition and results of operations.

#### CONTROL OF THE COMPANY BY PRINCIPAL STOCKHOLDER; DISPARATE VOTING RIGHTS

Robert Greenberg, Chairman of the Board and Chief Executive Officer, owns 65.0% of the outstanding Class B Common Stock of the Company. The holders of Class A Common Stock and Class B Common Stock have identical rights except that holders of Class A Common Stock are entitled to one vote per share while holders of Class B Common Stock are entitled to ten votes per share on all matters submitted to a vote of the stockholders. As a result, Mr. Greenberg holds approximately 63.4% of the aggregate number of votes eligible to be cast by the Company's stockholders. Therefore, Mr. Greenberg is able to control substantially all matters requiring approval by the stockholders of the Company, including the election of directors and the approval of mergers or other business combination transactions, and also has control over the management and affairs of the Company. As a result of such control, certain transactions are not possible without the approval of Mr. Greenberg, including proxy contests, tender offers, open market purchase programs or other transactions that can give stockholders of the Company the opportunity to realize a premium over the then-prevailing market prices for their shares of Class A Common Stock. The differential in the voting rights may adversely affect the value of the Class A Common Stock to the extent that investors or any potential future purchaser of the Company view the superior voting rights of the Class B Common Stock to have value.

#### ANTI-TAKEOVER PROVISIONS

The Company is subject to the anti-takeover provisions of Section 203 of the Delaware General Corporation Law. In general, Section 203 prevents an "interested stockholder" (defined generally as a person owning more than 15.0% or more of the Company's outstanding voting stock) from engaging in a "business combination" with the Company for three years following the date that person became an interested stockholder unless the business combination is approved in a prescribed manner. This statute could make it more difficult for a third party to acquire control of the Company.

The Board of Directors has the authority to issue up to 10,000,000 shares of Preferred Stock and to determine the rights, preferences, privileges and restrictions of such shares without any further vote or action by the stockholders. Although at present the Company has no plans to issue any shares of Preferred Stock, Preferred Stock could be issued with voting, liquidation,

dividend and other rights superior to the rights of the Common Stock. The issuance of Preferred Stock under certain circumstances could have the effect of delaying or preventing a change in control of the Company.

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Mr. Greenberg's substantial beneficial ownership position, together with the authorization of Preferred Stock, the disparate voting rights between the Class A and Class B Common Stock, the classification of the Board of Directors and the lack of cumulative voting in the Company's Certificate of Incorporation and Bylaws, may have the effect of delaying, deferring or preventing a change in control of the Company, may discourage bids for the Company's Class A Common Stock at a premium over the market price of the Class A Common Stock and may adversely affect the market price of the Class A Common Stock.

#### NO ASSURANCE OF ACTIVE TRADING MARKET FOR CLASS A COMMON STOCK AND POSSIBLE VOLATILITY OF STOCK PRICE

The market price of our Class A Common Stock has been extremely volatile. During 1999, the Company's Common Stock reached a high of \$11.81 per share and a low of \$3.44. On December 31, 1999, the closing market price was \$3.81 per share. The market price for shares of the Class A Common Stock may continue to fluctuate based upon a number of factors, including, without limitation, business performance, news announcements, quarterly fluctuations in the Company's financial results, changes in earnings estimates or recommendations by analysts or changes in general economic and market conditions.

If the Company's results of operations fail to meet the expectations of securities analysts or investors in a future quarter, the market price of our Class A Common Stock could also be materially adversely affected.

#### SHARES ELIGIBLE FOR FUTURE SALE; REGISTRATION RIGHTS

The sales of substantial amounts of the Company's Class A Common Stock in the public market or the prospect of such sales could materially and adversely affect the market price of the Class A Common Stock. The Company has outstanding 8,481,623 shares of Class A Common Stock. In addition, the Company has outstanding 26,423,445 shares of Class B Common Stock, all of which are convertible into Class A Common Stock on a share-for-share basis at the election of the holder or upon transfer or disposition to persons who are not Permitted Transferees (as defined in the Company's Certificate of Incorporation). The 8,481,623 shares of Class A Common Stock are eligible for sale in the public market without restriction. The 26,423,445 shares of Class B Common Stock are restricted in nature and are saleable pursuant to Rule 144 under the Securities Act of 1933, as amended (the "Securities Act"). Robert Greenberg, Chairman of the Board and Chief Executive Officer, and Michael Greenberg, President, beneficially own an aggregate of 20,860,613 shares of Class B Common Stock for which they have received certain registration rights to sell such shares of Class A Common Stock issuable upon conversion of their shares of Class B Common Stock in the public market. The Company also registered under the Securities Act shares of Class A Common Stock reserved for issuance pursuant to the Stock Option Plan and the 1998 Employee Stock Purchase Plan.

#### YEAR 2000 COMPLIANCE

The Company instituted a program to determine the internal readiness of its computer systems for handling the year 2000 ("Y2K") issue. Although management believes the Company adequately addressed Y2K compliance issues, and to date, there have not been any problems with the Company's computer systems and non-informational technology systems relating to Y2K compliance, there can be no assurance that such problems will not be identified in the future. However, the Company believes that it has sufficient resources and that any such problems subsequently identified will not be material to the Company's financial position or results of operations.

## ITEM 2. PROPERTIES

The Company's corporate headquarters and additional administrative offices are located at three premises in Manhattan Beach, California, and consist of an aggregate of approximately 35,000 square feet. The leases on the premises expire between February 2002 and February 2008, with options to extend in some cases, and the current aggregate annual rent is approximately \$1.1 million.

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The Company also leases space for its distribution centers and its retail stores. These facilities aggregate approximately 1.1 million square feet, with an annual aggregate base rental of approximately \$8.0 million, plus, in some cases, a percentage of the store's gross sales in excess of the base annual rent. The terms of these leases vary as to duration and rent escalation provisions. The Company has also signed leases for retail stores expected to be opened in 2000. In general, the leases expire between August 2000 and November 2010 and provide for rent escalations tied to either increases in the lessor's operating expenses or fluctuations in the consumer price index in the relevant geographical area.

## ITEM 3. LEGAL PROCEEDINGS

On April 16, 1999, a complaint captioned Swanier v. Skechers was filed against the Company and an employee of the Company in the Superior Court, County of Los Angeles, Southwest District, Torrance, Case No. YC034808. The complaint alleged various causes of action in connection with plaintiff's employment by the Company. The Complaint has since been settled, and the terms of the settlement did not have a material impact on the Company's financial position or results of its operations.

On June 14, 1999, a complaint captioned R. Griggs Group Limited v. Skechers U.S.A., Inc. was filed against the Company in the United States District Court, Northern District of California (San Francisco Division), Case No. 99-2862. R. Griggs Group Limited manufactures and markets footwear including Dr. Martens. The complaint alleged various causes of action, including Federal, state and common law unfair competition and Federal and state dilution, with respect to certain trade dress marks of certain styles of footwear, and fraud and deceit regarding the plaintiff's alleged postponement of the filing of the action. On June 15, 1999, the Company filed a complaint captioned Skechers U.S.A., Inc. v. R. Griggs Group Limited in the United States District Court, Central District of California (Los Angeles Division), Case No. 99-06115. The complaint sought a declaratory judgment of non-infringement, invalidity and unenforceability of defendant's trade dress rights and further declaratory judgment that the Company did not breach a trade dress settlement agreement previously entered into by and between the parties. The two complaints were resolved in February 2000. The parties have signed a letter of intent embodying the material terms of the settlement and are currently working on the final written agreement. The terms are confidential but the Company can disclose that the settlement will not require payment of any money by the Company. The non-monetary terms will not have a material impact on the Company's financial position or results of operations.

On December 29, 1999, a complaint captioned Shapiro, et al., v. Skechers U.S.A., Inc., et al. was filed against the Company and two of its officers and directors in the United States District Court, Central District of California, Case No. 99-13559. The complaint is a purported class action claiming damages for alleged violations of the Securities Act and the Securities Exchange Act of 1934, as amended (the "Securities Exchange Act"). The Shapiro complaint also names the underwriters for the Company's Initial Public Offering of its Class A Common Stock on June 9, 1999 (the "Offering") as defendants in the case. On January 12, 2000, a complaint captioned Abraham, et al., v. Skechers U.S.A., Inc., et al. was filed against the Company and two of its officers and directors in the

United States District Court, Central District of California, Case No. 00-00471. The complaint is a purported class action claiming damages for alleged violations of the Securities Act and Securities Exchange Act. On January 24, 2000, a complaint captioned *Astrolio, et al., v. Skechers U.S.A., Inc., et al.* was filed against the Company and two of its officers and directors in the United States District Court, Central District of California, Case No. 00-00772. The complaint is a purported class action claiming damages changes for alleged violations of the Securities Act and Securities Exchange Act. The Astrolio complaint also names the underwriters for the Offering as defendants in the case. On January 19, 2000, a complaint captioned *Pugliesi, et al., v. Skechers U.S.A., Inc., et al.* was filed against the Company and two of its officers and directors in the United States District Court, Central District of California, Case No. 00-00631. The complaint is a purported class action claiming damages for alleged violations of the Securities Act and the Securities Exchange Act.

Shapiro, Abraham, Astrolio, and Pugliesi (collectively, the "Skechers Securities Litigation") were each filed within the last three months, and no defendant as yet has filed a formal response. All of the complaints in the Skechers Securities Litigation seek both damages and rescission on behalf of a class of

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persons who purchased securities in, or traceable to, the Offering and / or thereafter on the open market prior to July 6, 1999. The four cases are expected to be consolidated. As these matters are in the early stages of discovery, neither the Company nor its counsel are able to conclude as to the potential likelihood of an unfavorable outcome. The Company is vigorously defending these complaints and believes their defenses to be meritorious. Accordingly, the Company has not provided for any potential losses associated with these lawsuits.

The Company occasionally becomes involved in litigation arising from the normal course of business. Other than the foregoing, management believes that any liability with respect to pending legal actions, individually or in the aggregate, will not have a material adverse effect on the Company's business, financial condition and results of operations.

#### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to the security holders to be voted on during the fourth quarter of 1999.

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## PART II

#### ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's Class A Common Stock began trading on the New York Stock Exchange on June 9, 1999 after the Company completed an initial public offering of 7,000,000 shares of Class A Common Stock at \$11.00 per share. The Company's Class A Common Stock trades under the symbol "SKX". The following table sets forth, for the periods indicated, the high and low sales prices of the Class A Common Stock.

Year Ended December 31, 1999:	High	Low
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Second Quarter (1)	\$11.81	\$ 9.75
Third Quarter	10.25	4.75
Fourth Quarter	5.19	3.44

(1) For the period from June 9, 1999 to June 30, 1999.

As of March 28, 2000, there were 63 holders of record of Class A Common Stock (including holders who are nominees for an undetermined number of beneficial owners) and 6 holders of record of the Company's Class B Common Stock. These figures do not include beneficial owners who hold shares in nominee name. The Class B Common Stock is not publicly traded but each share is convertible upon request of the holder into one share of Class A Common Stock.

In May 1992, the Company elected to be treated for Federal and state income tax purposes as an S Corporation under Subchapter S of the Internal Revenue Code of 1986, as amended (the "Code"), and comparable state laws. As a result, earnings of the Company, since such initial election, were included in the taxable income of the Company's stockholders for Federal and state income tax purposes, and the Company was not subject to income tax on such earnings, other than franchise and net worth taxes. Prior to the closing of the Offering, the Company terminated its S Corporation status, and since then the Company has been treated for Federal and state income tax purposes as a corporation under Subchapter C of the Code and, as a result, had become subject to state and Federal income taxes. By reason of the Company's treatment as an S Corporation for Federal and state income tax purposes, the Company, since inception, had provided to its stockholders funds for the payment of income taxes on the earnings of the Company. The Company declared distributions relating to its S Corporation status of \$7.9 million in 1998 and \$35.4 million in 1999 ("S Corporation Distributions"), \$21.0 million of which was paid from a portion of the net proceeds of the Offering.

In connection with the Offering and the termination of the Company's S Corporation tax status, the Company entered into a tax indemnification agreement with each of its stockholders. The agreement provides that the Company will indemnify and hold harmless each of the stockholders for Federal, state, local or foreign income tax liabilities, and costs relating thereto, resulting from any adjustment to the Company's taxable income that is the result of an increase in or change in character of, the Company's income during the period it was treated as an S Corporation up to the Company's tax savings in connection with such adjustments. The agreement also provides that if there is a determination that the Company was not an S Corporation prior to the Offering, stockholders will indemnify the Company for the additional tax liability arising as a result of such determination. The stockholders will also indemnify the Company for any increase in the Company's tax liability to the extent such increase results in a related decrease in the stockholders' tax liability.

Purchasers of shares of Class A Common Stock in the Offering did not receive any portion of the S Corporation Distributions. The Company has

never declared or paid dividends on its Class A Common Stock. The Company currently intends to retain any earnings for use in its business and does not anticipate paying any cash dividends in the foreseeable future.

#### ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following tables set forth selected consolidated financial data of the Company as of and for each of the years in the five-year period ended December 31, 1999.



SUMMARY FINANCIAL DATA  
(In thousands, except earnings per share)

	Years ended December 31,				
	1995	1996	1997	1998	1999
<b>STATEMENT OF OPERATION DATA:</b>					
Net sales	\$ 110,649	\$ 115,410	\$ 183,827	\$ 372,680	\$ 424,601
Gross profit	31,957	34,211	68,723	154,580	174,608
Operating expenses:					
Selling	12,150	11,739	21,584	49,983	57,332
General and administrative	19,850	18,939	32,397	71,461	79,114
Earnings from operations	1,800	5,125	15,636	33,991	38,830
Interest expense	3,676	3,231	4,186	8,631	6,554
Earnings (loss) before income taxes and extraordinary credit	(1,662)	1,955	11,413	25,121	32,691
Net earnings (loss)	(1,222) (1)	1,910	11,023	24,471	24,056
<b>PRO FORMA OPERATIONS DATA: (2)</b>					
Earnings (loss) before income taxes and extraordinary credit	\$ (1,662)	\$ 1,955	\$ 11,413	\$ 25,121	\$ 32,691
Income taxes (benefit)	(665)	782	4,565	10,048	12,880
Net earnings (loss)	(727) (1)	1,173	6,848	15,073	19,811
Net earnings (loss) per share: (3)					
Basic	\$ (0.03)	\$ 0.04	\$ 0.25	\$ 0.54	\$ 0.62
Diluted	\$ (0.02)	\$ 0.04	\$ 0.23	\$ 0.49	\$ 0.60
Weighted average shares: (3)					
Basic	27,814	27,814	27,814	27,814	31,765
Diluted	29,614	29,614	29,614	30,610	33,018

	As of December 31,				
	1995	1996	1997	1998	1999
<b>BALANCE SHEET DATA:</b>					
Working capital	\$ 8,155	\$ 11,987	\$ 17,081	\$ 23,106	\$ 65,003
Total assets	47,701	42,151	90,881	146,284	177,914
Total debt	31,748	25,661	39,062	70,933	33,950
Stockholders' equity	938	3,336	11,125	27,676	86,000

- (1) Includes an extraordinary gain of \$443,000 net of state income taxes of \$7,000 (\$270,000 on a pro forma basis, net of \$180,000) resulting from the acceleration of the repayment of a note.
- (2) Reflects adjustments for Federal and state income taxes assuming the Company had been taxed as a C Corporation rather than as an S Corporation.
- (3) Basic earnings per share represents net earnings divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if options to issue common stock were exercised or converted into common stock. The weighted average diluted shares outstanding gives effect to the sale by the Company of those shares of common stock necessary to fund the payment of (i) stockholder distributions paid or declared from January 1, 1998 to June 7, 1999, the S Corporation termination date, in excess of (ii) the S Corporation earnings from January 1, 1998 to December 31, 1998 for both 1997 and 1998, and January 1, 1999 to June 7, 1999 for 1999, based on an initial public offering price of \$11 per share, net of underwriting discounts.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Certain information contained in the following Management's Discussion and

Analysis of Financial Condition and Results of Operations constitute forward-looking statements within the meaning of the Securities Act and the Securities Exchange Act, which can be identified by the use of forward-looking terminology such as "believes," "anticipates," "plans," "expects," "may," "will," "intends," "estimates" and similar expressions that are intended to identify forward-looking statements. These forward-looking statements involve risks and uncertainties, and the Company's actual results may differ materially from the results discussed in the forward-looking statements as a result of certain factors set forth in "Risk Factors" and elsewhere in this Report.

#### OVERVIEW

The Company has realized rapid growth since inception, increasing net sales at a compound annual growth rate of 36.2% from \$90.8 million in 1994 to \$424.6 million in 1999. Significant growth was experienced in 1998, when the Company experienced a 102.7% and 117.4% increase in sales and earnings from operations, respectively. This momentum continued into 1999 with a 13.9% increase in sales and a 14.2% increase in earnings from operations. From 1997 to 1998, the Company also experienced an improvement in Gross Margin from 37.4% to 41.5% and was able to maintain these margins at a comparable level in 1999 of 41.1%. Operating Margin also increased from 8.5% in 1997 to 9.1% in 1998 and 9.1% in 1999. These improvements resulted in part from the shift to offering Skechers product exclusively (away from the "Cross Colours", "Karl Kani" and "So...LA" brands) and in part from economies of scale. In the future, the Company's rate of growth will be dependent upon, among other things, the continued success of its efforts to expand its footwear offerings within the Skechers brand or developing alternative, successful brands. There can be no assurance that the rate of growth will not decline in future periods or that the Company will improve or maintain Operating Margins.

As the Company's sales growth has accelerated, management has focused on investing in infrastructure to support continued expansion in a disciplined manner. Major areas of investment have included expanding the Company's distribution facilities, hiring additional personnel, developing product sourcing and quality control offices in Taiwan, upgrading the Company's management information systems, developing and expanding the Company's retail stores and launching its direct mail business in August 1998 through its web site and catalog. The Company has established this infrastructure to achieve further economies of scale in anticipation of continued increases in sales. Because expenses relating to this infrastructure are fixed, at least in the short-term, operating results and margins would be adversely affected if the Company does not achieve anticipated continued growth.

Management has implemented a strategy of controlling the growth of the distribution channels through which the Company's products are sold in order to protect the Skechers brand name, properly service customer accounts and better manage the growth of the business. Increasing sales depend on various factors, including strength of the Company's brand name, competitive conditions, the ability of the Company to manage the increased sales and stores. There can be no assurance that the Company's growth strategy will be successful or that the Company's sales or earnings will increase as a result of the implementation of such efforts.

As of February 29, 2000 the Company operated 23 concept stores at marquee locations in major metropolitan cities. Each concept store serves not only as a showcase for the Company's full product offering for the current season but also as a rapid product feedback mechanism. Product sell-through information derived from the Company's concept stores enables the Company's sales, merchandising and production staff to respond to market changes and new product introductions. Such responses serve to augment sales and limit inventory markdowns and customer

returns and allowances. As of February 29, 2000, the Company also operated 19 factory and warehouse outlet stores that enable the Company to liquidate excess, discontinued and odd-size inventory in a cost efficient manner. The Company plans to increase the number of retail locations in the future to further its strategic goals as well as in an effort to increase sales and earnings. The Company plans to open at least three new concept stores and six new outlet stores in the remainder of 2000.

Although the Company's primary focus is on the domestic market, the Company presently markets its product in countries in Europe, Asia and selected other foreign regions through distributorship agreements. To date, international sales have been made in U.S. Dollars, although there can be no assurance that this will continue to be the case. The Company's goal is to increase sales through distributors by heightening the Company's marketing support in these countries. Sales through foreign distributors have resulted in lower gross margins to the Company than domestic sales. To the extent that the Company expands its international operations through distribution arrangements, its overall gross margins may be adversely affected. In 1998, the Company launched its first major international advertising campaign in Europe and Asia. In an effort to increase profit margins on products sold internationally and more effectively promote the Skechers brand name, the Company is exploring selling directly to retailers in certain European countries in the future. In addition, the Company is exploring selectively opening flagship retail stores internationally on its own or through joint ventures. There can be no assurance that such expansion plans will be successful.

Management believes that selective licensing of the Skechers brand name to non-footwear-related manufacturers may broaden and enhance the Skechers image without requiring significant capital investments or the incurrence of significant incremental operating expenses by the Company. The Company is experimenting with certain manufacturers on very limited basis to study the potential impact of licensing its brand name. To date, there has not been any significant royalty income from such licensing agreements.

The Company contracts with third parties for the manufacture of all of its products. The top four manufacturers of the Company's products in 1999 accounted for 15.5%, 13.4%, 13.3% and 12.3% of total purchases, respectively. During 1998, the Company had four manufacturers which accounted for 15.4%, 14.2%, 12.1%, and 10.4% of total purchases, respectively, and in 1997, the Company had two manufacturers which accounted for 21.7% and 15.0% of total purchases, respectively. To date, products have been purchased in U.S. Dollars, although there can be no assurance that this will continue to be the case. The Company believes the use of independent manufacturers increases its production flexibility and capacity while at the same time allowing the Company to substantially reduce capital expenditures and avoid the costs of managing a large production work force. Substantially all of the

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Company's products are produced in China. The Company finances its production activities in part through the use of interest-bearing open purchase arrangements with certain of its Asian manufacturers. These facilities currently bear interest at a rate between 1.5% for 30 day financing and 2.0% for 45 to 60 day financing (depending on the factory). Management believes that the use of these arrangements affords the Company additional liquidity and flexibility. Finished goods are received, inspected and shipped to domestic accounts primarily from the Company's distribution centers located in Ontario, California. Substantially all of the international orders are shipped directly from the manufacturer to Skechers' international distributors.

In May 1992, the Company elected to be treated for Federal and state income tax purposes as an S Corporation under Subchapter S of the Code and comparable state laws. As a result, earnings of the Company, since such initial election, were included in the taxable income of the Company's stockholders for Federal and state income tax purposes, and the Company was not subject to income tax on such earnings, other than franchise and net worth taxes. Since the termination of the Company's S Corporation status on June 7, 1999, the Company has been treated for

Federal and state income tax purposes as a corporation under Subchapter C of the Code and, as a result, became subject to state and Federal income taxes. By reason of the Company's treatment as an S Corporation for Federal and state income tax purposes, the Company, since inception, has made distributions to its stockholders to include the payment of income taxes on the earnings of the Company as well as the taxes payable when the Company's converted to a C Corporation. The Company declared S Corporation Distributions of \$7.9 million in 1998 and \$35.4 million in 1999, \$21.0 million of which was paid from a portion of the net proceeds of the Offering.

YEAR ENDED DECEMBER 31, 1999 COMPARED TO THE YEARS ENDED DECEMBER 31, 1998 AND 1997

#### Net Sales

Net sales increased by \$51.9 million to \$424.6 million, an increase of 14.0%. This compares to an increase of \$188.9 million, or 102.7%, to \$372.7 million for the 1998 as compared to \$183.8 million for 1997. Continued growth in sales of branded footwear is primarily as a result of (i) greater brand awareness driven in part by a continued expansion of the Company's national marketing efforts, (ii) a broader breadth of men's, women's and children's product offerings, (iii) the development of the Company's domestic and international sales forces and (iv) the transition of the Company's account base in the direction of larger accounts with multiple stores and increased sales to such accounts, resulting in higher sales per account.

During 1999, the Company was able to successfully target additional styles and categories in the moderately-priced footwear market. Wholesale units sold increased 20.5% from 16.1 million units in 1998 to 19.4 million units in 1999. The Company was able to accomplish this and still maintain its gross margin at a level comparable to that achieved in 1998 by carefully targeting production and inventory levels with the level of orders from customers. In addition, it was able to better match styles with seasonal trends during 1999. During 1998, the increase in unit sales was 106.4%, from 7.8 million units in 1997 to 16.1 million units in 1998, compared to a sales increase of 102.7%.

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#### Gross Profit

The Company's gross profit increased \$20.0 million, or 13.0%, to \$174.6 million in 1999 compared to \$154.6 million in 1998. In 1998, gross profit increased \$85.9 million, or 124.9%, to \$154.6 million compared to \$68.7 million in 1997. Gross margin increased from 37.4% in 1997 to 41.5% in 1998, but remained relatively constant at 41.1% in 1999. The increase in the gross margin in 1998 was primarily due to (i) an increase in the proportions of total sales derived from the women's and children's footwear line, which had a higher gross margin than the men's footwear line, (ii) better retail sell-through at the Company's retail customer accounts, which typically results in fewer markdowns and (iii) an increase in the Company's retail store sales, since such retail gross margins are higher than wholesale gross margins and

#### Selling Expenses

Selling expenses increased \$7.3 million, or 14.7%, to \$57.3 million in 1999 compared to \$50.0 million in 1998. As a percentage of net sales, selling expenses remained relatively constant in 1999 at 13.5% compared to 13.4% in 1998. Selling expenses increased \$28.4 million, or 131.6%, to \$50.0 million for 1998 from \$21.6 million (11.7% of net sales) for 1997. The increase during 1998 was primarily due to increased advertising expenditures and sales compensation due to the increase in footwear sales, the implementation of a new sales compensation package and the hiring of additional sales personnel. Advertising expenses as a percentage of sales for 1999, 1998 and 1997 was 11.2%, 11.3% and 8.6%, respectively.

## General and Administrative Expenses

General and administrative expenses increased \$7.7 million to \$79.1 million in 1999, compared to \$71.5 million in 1998. As a percentage of sales, general and administrative expenses decreased to 18.6% from 19.2%. In 1998, general and administrative expenses increased \$39.1 million, or 120.6%, to \$71.5 million for 1998 from \$32.4 million (17.6% of net sales) for 1997. The increase in total dollars and as a percentage of sales in 1998 is primarily due to (i) the hiring of additional personnel, (ii) an increase in costs associated with the Company's distribution facilities to support the Company's growth, (iii) increased product design and development costs, (iv) the addition of 23 retail stores which were not open in 1997, and (v) increased discretionary expenses consisting of bonuses paid to an executive officer and certain employees. Also included in general and administrative expenses in 1998 and 1997 are \$7.0 million and \$2.7 million, respectively, of bonus compensation expense related to the Company's 1996 Incentive Compensation Plan. In 1999, \$1.2 million in bonuses were paid on discretionary basis by the board.

## Interest Expense

Interest expense decreased to \$6.6 million in 1999 from \$8.6 million in 1998 as a result of a reduction in borrowings under the Company's revolving line of credit and the repayment of the \$10.0 million note payable to a stockholder. From 1997 to 1998, interest expense increased \$4.4 million, or 106.2%, to \$8.6 million for 1998 as compared to \$4.2 million for 1997 as a result of increased borrowings to fund the Company's expanded operations and interest expense associated with open purchase arrangements with certain of the Company's Asian manufacturers, which in part finance the Company's manufacturing activities.

## Pro Forma Income Taxes

Pro forma income taxes represent taxes, which would have been reported assuming the Company been subject to federal and state taxes as a C Corporation.

## LIQUIDITY AND CAPITAL RESOURCES

Up until the completion of the Offering in June, 1999, the Company relied upon internally generated funds, trade credit, borrowings under credit facilities and loans from a stockholder to finance its operations and expansion. The Company's need for funds arises primarily from its working capital requirements, including the need to finance its inventory and receivables. The Company's working capital was \$65.0 million at December 31, 1999 as compared to \$23.1 million at December 31, 1998. This increase in working capital was primarily due to the proceeds, after distribution to stockholders, of the proceeds from the Offering in June 1999, offset in part by the requirements to continue to fund the Company's growth and expansion in 1999.

As part of the Company's working capital management, the Company performs substantially all customer credit functions internally, including extension of credit and collections. The Company's bad debt write-offs were less than 1.0% of net sales for 1999 and 1998. The Company carries bad debt insurance to cover approximately the first 90.0% of bad debts on substantially all of the Company's major retail accounts.

Net cash provided by operating activities totaled \$13.1 million during 1999, compared to net cash used in operating activities of \$4.3 million for 1998. The increase in cash provided by operating activities was due to a reduction in the buildup of inventory levels (a decrease in inventory balances as a percentage of sales).

Net cash used in investing activities totaled \$10.8 million and \$9.4 million for 1999 and 1998, respectively, and related to capital expenditures. Capital

expenditures were principally expended in connection with the establishment of the Company's distribution center in Ontario, California, additional hardware and software for the Company's computer needs as well as the addition of retail stores. Capital expenditures for 1999 included approximately \$5.5 million used for the installation of a new material handling system, expected to be completed in 2000, for the Company's most recently opened distribution facility, the total of which is expected to be approximately \$12.0 million.

Net cash used in financing activities totaled \$2.4 million in 1999, compared to cash flow provided by financing activities of \$23.2 million in 1998. The decrease in cash from financing activities was primarily due to reduced financing needs to fund growth (a corresponding increase in cash flow from operations and funds available from initial public offering of \$69.7 million).

The Company's credit facility provides for borrowings under a revolving line of credit of up to \$120.0 million and a term loan, with actual borrowings limited to available collateral and certain limitations on total indebtedness (approximately \$39.5 million of availability as of December 31, 1999) with The CIT Group, as agent for the lenders. As of December 31, 1999, there was approximately \$30.4 million outstanding under the revolving line of credit. The revolving line of credit bears interest at the Company's option at either the prime rate (8.5% at December 31, 1999) plus 25 basis points or at Libor (6.0% at December 31, 1999) plus 2.75%. The revolving line of credit expires on December 31, 2002. Interest on the revolving line of credit is payable monthly in arrears. The revolving line of credit provides a sub-limit for letters of credit of up to \$18.0 million to finance the Company's foreign purchases of merchandise inventory. As of December 31, 1999, the Company had approximately \$4.4 million of letters of credit under the revolving line of credit. The term loan component of the credit facility, which has a principal balance of approximately \$2.4 million as of December 31, 1999, bears interest at the prime rate plus 100

basis points and is due in monthly installments of \$25,000 with a final balloon payment December 2002. The proceeds from this note were used to purchase equipment for the Company's distribution centers in Ontario, California and the note is secured by such equipment. The credit facility contains certain financial covenants that require the Company to maintain minimum tangible net worth of at least \$20.0 million, working capital of at least \$14.0 million and specified leverage ratios and limit the ability of the Company to pay dividends if it is in default of any provisions of the credit facility. The Company was in compliance with these covenants as of December 31, 1999. The credit facility is collateralized by the Company's real and personal property, including, among other things, accounts receivable, inventory, general intangibles and equipment and is guaranteed by the Company's wholly-owned subsidiaries.

As of December 31, 1998, the Company had an unsubordinated note payable to the Greenberg Family Trust in the amount of \$10.0 million. The Company recorded interest expense of approximately \$433,000, \$540,000 and \$1.1 million related to notes payable to the Greenberg Family Trust during the years ended December 31, 1999, 1998 and 1997, respectively. This note was repaid during 1999, with the proceeds, in part, from the Offering.

By reason of the Company's treatment as an S Corporation for Federal and state income tax purposes, the Company since inception provided to its stockholders funds for the payment of income taxes on the earnings of the Company as well as the conversion from an S Corporation to a C Corporation during 1999. The Company declared S Corporation Distributions of \$35.4 million, \$7.9 million and \$3.2 million in 1999, 1998 and 1997, respectively. Since the termination of the Company's S Corporation status, earnings have been and will be retained for the foreseeable future in the operations of the business.

The Company believes that anticipated cash flows from operations, available

borrowings under the Company's revolving line of credit, cash on hand and its financing arrangements will be sufficient to provide the Company with the liquidity necessary to fund its anticipated working capital and capital requirements through fiscal 2000. However, in connection with its growth strategy, the Company will incur significant working capital requirements and capital expenditures. The Company's future capital requirements will depend on many factors, including, but not limited to, the levels at which the Company maintains inventory, the market acceptance of the Company's footwear, the levels of promotion and advertising required to promote its footwear, the extent to which the Company invests in new product design and improvements to its existing product design and the number and timing of new store openings. To the extent that available funds are insufficient to fund the Company's future activities, the Company may need to raise additional funds through public or private financing. No assurance can be given that additional financing will be available or that, if available, it can be obtained on terms favorable to the Company and its stockholders. Failure to obtain such financing could delay or prevent the Company's planned expansion, which could adversely affect the Company's business, financial condition and results of operations. In addition, if additional capital is raised through the sale of additional equity or convertible securities, dilution to the Company's stockholders could occur.

#### INFLATION

The Company does not believe that the relatively moderate rates of inflation experienced in the United States over the last three years have had a significant effect on its sales or profitability. However, the Company cannot accurately predict the effect of inflation on future operating results. Although higher rates of inflation have been experienced in a number of foreign countries in which the Company's products are manufactured, the Company does not believe that inflation has had a material effect on the Company's sales or profitability. In the past, the Company has been able to offset its foreign product cost increases by increasing prices or changing suppliers, although no assurance can be given that the Company will be able to continue to make such increases or changes in the future.

#### EXCHANGE RATES

The Company receives U.S. Dollars for substantially all of its product sales and its royalty income. Inventory purchases from offshore contract manufacturers are primarily denominated in U.S. Dollars; however, purchase prices for the Company's products may be impacted by fluctuations in the exchange rate

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between the U.S. Dollar and the local currencies of the contract manufacturers, which may have the effect of increasing the Company's cost of goods in the future. During 1998 and 1999, exchange rate fluctuations did not have a material impact on the Company's inventory costs. The Company does not engage in hedging activities with respect to such exchange rate risk.

#### MARKET RISK

The Company does not hold any derivative securities or other market rate sensitive instruments.

#### YEAR 2000 COMPLIANCE

In prior years, the Company discussed the nature and progress of its plans to become Year 2000 ("Y2K") compliant. As a result of those planning and implementation efforts, the Company experienced no significant disruptions in mission critical information technology and non-information technology systems and believes those systems have successfully responded to the Y2K date change. The Company's costs associated with becoming Y2K compliant were less than \$100,000 exclusive of system upgrades incurred in the normal course of business. The Company is not aware of any material problems resulting from Y2K issues, either with its products, its internal systems or the products and services of

third parties. The potential inability of third parties to address their own Y2K issues remains a risk which is difficult to assess. The Company will continue to monitor its mission critical computer applications and those of its suppliers and vendors throughout the Y2K to ensure that any latent Y2K matters that may arise are addressed promptly.

#### FUTURE ACCOUNTING CHANGES

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 133, Accounting for Derivative Instruments and Hedging Activities ("SFAS No. 133"). SFAS No. 133 modifies the accounting for derivative and hedging activities and is effective for fiscal years beginning after June 15, 2000. Since the Company does not presently hold any derivatives or engage in hedging activities, accordingly SFAS No. 133 should not impact the Company's financial position or results of operations.

#### ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The information required by this Item 8 is incorporated by reference to Skechers U.S.A., Inc.'s Consolidated Financial Statements and Independent Auditors' Report beginning at page F-1 of this Form 10-K.

#### ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

#### ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by this Item 10 is hereby incorporated by reference from Skechers U.S.A., Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Skechers U.S.A., Inc.'s 1999 fiscal year.

#### ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item 11 is hereby incorporated by reference from Skechers U.S.A., Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Skechers U.S.A., Inc.'s 1999 fiscal year.

#### ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The information required by this Item 11 is hereby incorporated by reference from Skechers U.S.A., Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Skechers U.S.A., Inc.'s 1999 fiscal year.

#### ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this Item 11 is hereby incorporated by reference from Skechers U.S.A., Inc.'s definitive proxy statement, to be filed pursuant to Regulation 14A within 120 days after the end of Skechers U.S.A., Inc.'s 1999 fiscal year.

#### PART IV

#### ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

- (a) Consolidated financial statements and schedules required to be filed hereunder are indexed on Page F-1 hereof.
- (b) Reports on Form 8K ---There were no reports on Form 8-K filed during the last quarter of the fiscal year ended December 31, 1999.



EXHIBIT NUMBER	DESCRIPTION OF EXHIBIT
2.1	Agreement of Reorganization and Plan of Merger (incorporated by reference to exhibit number 3.2(a) of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on May 12, 1999).
3.1	Certificate of Incorporation (incorporated by reference to exhibit number 3.1 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
3.2	Bylaws (incorporated by reference to exhibit number 3.2 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
3.2(a)	Amendment to Bylaws (incorporated by reference to exhibit number 3.2(a) of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on May 12, 1999).
4.1	Form of Specimen Class A Common Stock Certificate (incorporated by reference to exhibit number 4.1 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on May 12, 1999).
10.1	Amended and Restated 1998 Stock Option, Deferred Stock and Restricted Stock Plan (incorporated by reference to exhibit number 10.1 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
10.2	1998 Employee Stock Purchase Plan (incorporated by reference to exhibit number 10.2 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on May 12, 1999).
10.2(a)	Amendment to 1998 Employee Stock Purchase Plan (incorporated by reference to exhibit number 10.2(a) of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on June 7, 1999).

EXHIBIT NUMBER	DESCRIPTION OF EXHIBIT
10.3	Employment Agreement dated June 14, 1999, between the Registrant and Robert Greenberg (incorporated by reference to exhibit number

10.3 of the Registrant's Registration Statement on Form 10-Q, for the period ending June 30, 1999).

- 10.3(a) Amendment No. 1 to Employment Agreement between the Registrant and Robert Greenberg dated December 31, 1999.
- 10.4 Employment Agreement dated June 14, 1999, between the Registrant and Michael Greenberg (incorporated by reference to exhibit number 10.4 of the Registrant's Registration Statement on Form 10-Q, for the period ending June 30, 1999).
- 10.4(a) Amendment to Employment Agreement between the Registrant and Michael Greenberg dated December 31, 2000.
- 10.5 Employment Agreement dated June 14, 1999, between the Registrant and David Weinberg (incorporated by reference to exhibit number 10.5 of the Registrant's Registration Statement on Form 10-Q, for the period ending June 30, 1999).
- 10.5(a) Amendment No. 1 to Employment Agreement between the Registrant and David Weinberg dated December 31, 2000.
- 10.6 Indemnification Agreement dated June 7, 1999 between the Registrant and its directors and executive officers.
- 10.6(a) List of Registrant's directors and executive officers who entered into Indemnification Agreement referenced in Exhibit 10.6 with the Registrant.
- 10.7 Registration Rights Agreement dated June 9, 1999, between the Registrant, the Greenberg Family Trust, and Michael Greenberg (incorporated by reference to exhibit number 10.7 of the Registrant's Registration Statement on Form 10-Q, for the period ending June 30, 1999).
- 10.8 Tax Indemnification Agreement dated June 8, 1999, between the Registrant and certain shareholders (incorporated by reference to exhibit number 10.8 of the Registrant's Registration Statement on Form 10-Q, for the period ending June 30, 1999).
- 10.9 Subordinated Promissory Note between the Registrant and the Greenberg Family Trust, dated December 22, 1998 (incorporated by reference to exhibit number 10.9 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
- 10.10 Amended and Restated Loan and Security Agreement between the Registrant and Heller Financial, Inc., dated September 4, 1998 (incorporated by reference to exhibit number 10.10 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
- 10.10(a) Term Loan A Note, dated September 4, 1998, between the Registrant and Heller Financial, Inc. (incorporated by reference to exhibit number 10.10(a) of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
- 10.10(b) Revolving Note dated September 4, 1998, between the Registrant and Heller Financial, Inc. (incorporated by reference to exhibit number 10.10(b) of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
- 10.10(c) First Amendment to Amended and Restated Loan and Security Agreement, dated September 11, 1998 (incorporated by reference to exhibit number 10.10(c) of the Registrant's Registration

Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).

EXHIBIT NUMBER	DESCRIPTION OF EXHIBIT
10.10(d)	Second Amendment to Amended and Restated Loan and Security Agreement, dated December 23, 1998 (incorporated by reference to exhibit number 10.10(d) of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
10.11	Lease, dated April 15, 1998, between the Registrant and Holt/Hawthorn and Victory Partners, regarding 228 Manhattan Beach Boulevard, Manhattan Beach, California (incorporated by reference to exhibit number 10.11 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
10.12	Commercial Lease Agreement, dated February 19, 1997, between the Registrant and Richard and Donna Piazza, regarding 1110 Manhattan Avenue, Manhattan Beach, California (incorporated by reference to exhibit number 10.12 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
10.13	Lease, dated June 12, 1998, between the Registrant and Richard and Donna Piazza, regarding 1112 Manhattan Avenue, Manhattan Beach, California (incorporated by reference to exhibit number 10.13 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
10.14	Lease, dated November 21, 1997, between the Registrant and The Prudential Insurance Company of America, regarding 1661 So. Vintage Avenue, Ontario, California (incorporated by reference to exhibit number 10.14 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
10.15	Lease, dated November 21, 1997, between the Registrant and The Prudential Insurance Company of America, regarding 1777 So. Vintage Avenue, Ontario, California (incorporated by reference to exhibit number 10.15 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
10.16	Commercial Lease, dated April 10, 1998, between the Registrant and Proficiency Ontario Partnership, regarding 5725 East Jurupa Street (incorporated by reference to exhibit number 10.16 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on July 29, 1998).
10.17	Lease and Addendum, dated June 11, 1998, between the Registrant and Delores McNabb, regarding Suite 3 on the first floor of the north building, Suite 9 on the first floor of the south building

at 904 Manhattan Avenue, Manhattan Beach, California (incorporated by reference to exhibit number 10.17 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).

- 10.18 Addendum to Lease, dated September 14, 1998, between the Registrant and Delores McNabb, regarding Suites 3, 4 and 5 on the second floor of the north building at 904 Manhattan Avenue, Manhattan Beach California (incorporated by reference to exhibit number 10.18 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
- 10.19 Promissory Note between the Registrant and the Greenberg Family Trust, dated December 22, 1998 (incorporated by reference to exhibit number 10.19 of the Registrant's Registration Statement on Form S-1, as amended (File No. 333-60065), filed with the Securities and Exchange Commission on April 9, 1999).
- 10.20 Lease, dated October 15, 1999, between the Registrant and Champagne Building Group LP, regarding 1670 South Champagne Avenue, Ontario, California.
- 10.21 Lease, dated November 18, 1999, between the Registrant and Pacifica California/Apollo, LLC, regarding Suites 125, 300, and 330 at 225 South Sepulveda Boulevard, Manhattan Beach, California.
- 10.22 Lease, dated July 1, 1999, between the Registrant and Richard and Donna Piazza, regarding 1108-B Manhattan Avenue, Manhattan Beach, California.
- 21.1 Subsidiaries of the Registrant

EXHIBIT NUMBER	DESCRIPTION OF EXHIBIT
23.1	Consent of KPMG LLP
24.1	Power of Attorney (included on signature page)
27	Financial Data Schedule

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, in the City of Manhattan Beach, State of California on the 30th day of March, 2000.

By: /s/ Robert Greenberg

-----  
Robert Greenberg  
Chairman of the Board  
and Chief Executive Officer

POWER OF ATTORNEY

We, the undersigned officers and directors of Skechers U.S.A., Inc., do hereby constitute and appoint Robert Greenberg, Michael Greenberg and David Weinberg, or either of them, our true and lawful attorneys and agents, to do any and all acts and things in our names in the capacities indicated below, which said attorneys and agents, or either of them, may deem necessary or advisable to enable said corporation to comply with the Securities Exchange Act of 1934, as amended, and any rules, regulations, and requirements of the Securities and Exchange Commission, in connection with this report, including specifically, but without limitation, power and authority to sign for us or any of us in our names and in the capacities indicated below, any and all amendments to this report, and we do hereby ratify and confirm all that the said attorneys and agents, or either of them, shall do or cause to be done by virtue hereof.

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

SIGNATURE -----	TITLE -----	DATE -----
/s/ ROBERT GREENBERG ----- Robert Greenberg	Chairman of the Board and Chief Executive Officer (Principal Executive Officer)	March 30, 2000
/s/ MICHAEL GREENBERG ----- Michael Greenberg	President and Director	March 30, 2000
/s/ DAVID WEINBERG ----- David Weinberg	Executive Vice President, Chief Financial Officer and Director (Principal Financial and Accounting Officer)	March 30, 2000
----- John Quinn	Director	March , 2000
----- Richard Siskind	Director	March , 2000

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INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders  
Skechers U.S.A., Inc.:

We have audited the accompanying consolidated financial statements of Skechers U.S.A., Inc. and subsidiaries as listed in the accompanying index. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Skechers U.S.A., Inc. and subsidiaries as of December 31, 1998 and 1999 and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1999 in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

Los Angeles, California  
February 29, 2000

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## SKECHERS U.S.A., INC.

## Consolidated Balance Sheets

December 31, 1998 and 1999

(In thousands, except per share data)

ASSETS	1998	1999
	-----	-----
Current assets:		
Cash	\$ 10,942	10,836
Trade accounts receivable, less allowances for bad debts and returns of \$3,413 in 1998 and \$3,237 in 1999	46,771	63,052
Due from officers and employees	116	851
Other receivables	2,329	2,771
	-----	-----
Total receivables	49,216	66,674
	-----	-----
Inventories	65,390	68,959
Prepaid expenses and other current assets	2,616	5,130
Deferred tax assets	--	2,810
	-----	-----
Total current assets	128,164	154,409
Property and equipment, at cost, less accumulated depreciation and amortization	15,196	21,387
Intangible assets, at cost, less applicable amortization	1,003	663
Other assets, at cost	1,921	1,455
	-----	-----
	\$146,284	177,914
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Short-term borrowings	\$ 54,323	30,382
Current installments of long-term borrowings	816	1,060
Current installments of notes payable to stockholder	2,244	--
Accounts payable	38,145	47,696
Accrued expenses	9,530	10,268
	-----	-----
Total current liabilities	105,058	89,406
	-----	-----
Long-term borrowings, excluding current installments	3,550	2,508
Notes payable to stockholder, excluding current installments	10,000	--
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$.001 par value. Authorized 10,000 shares; none issued and outstanding	--	--
Class A Common stock, \$.001 par value. Authorized 100,000 shares; issued and outstanding 7,091 shares at December 31,		

1999	--	7
Class B Common stock, \$.001 par value. Authorized 60,000 shares; issued and outstanding 27,814 shares	2	28
Additional paid-in capital	--	69,948
Retained earnings	27,674	16,017
	-----	-----
Total stockholders' equity	27,676	86,000
	-----	-----
	\$146,284	177,914
	=====	=====

See accompanying notes to consolidated financial statements.

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SKECHERS U.S.A., INC.

Consolidated Statements of Earnings

Three-year period ended December 31, 1999

(In thousands, except per share data)

	1997	1998	1999
	-----	-----	-----
Net sales	\$ 183,827	372,680	424,601
Cost of sales	115,104	218,100	249,993
	-----	-----	-----
Gross profit	68,723	154,580	174,608
Royalty income, net	894	855	668
	-----	-----	-----
	69,617	155,435	175,276
	-----	-----	-----
Operating expenses:			
Selling	21,584	49,983	57,332
General and administrative	32,397	71,461	79,114
	-----	-----	-----
	53,981	121,444	136,446
	-----	-----	-----
Earnings from operations	15,636	33,991	38,830
	-----	-----	-----
Other income (expense):			
Interest	(4,186)	(8,631)	(6,554)
Other, net	(37)	(239)	415
	-----	-----	-----
	(4,223)	(8,870)	(6,139)
	-----	-----	-----
Earnings before income taxes	11,413	25,121	32,691
Income taxes	390	650	8,635
	-----	-----	-----
Net earnings	\$ 11,023	24,471	24,056
	=====	=====	=====

Pro forma operations data:



Earnings before income taxes	\$ 11,413	25,121	32,691
Income taxes	4,565	10,048	12,880
	-----	-----	-----
Net earnings	\$ 6,848	15,073	19,811
	=====	=====	=====
Net earnings per share:			
Basic	\$ 0.25	0.54	0.62
Diluted	0.23	0.49	0.60
	=====	=====	=====
Weighted-average shares:			
Basic	27,814	27,814	31,765
Diluted	29,614	30,610	33,018
	=====	=====	=====

See accompanying notes to consolidated financial statements.

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SKECHERS U.S.A., INC.

Consolidated Statement of Stockholders' Equity

Three-year period ended December 31, 1999

(In thousands)

	COMMON STOCK						TOTAL STOCKHOLDERS' EQUITY
	SHARES		AMOUNT		ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	
	CLASS A	CLASS B	CLASS A	CLASS B			
Balance at December 31, 1996	--	27,814	\$ --	2	--	3,334	3,336
Net earnings	--	--	--	--	--	11,023	11,023
S Corporation distribution	--	--	--	--	--	(3,234)	(3,234)
	-----	-----	-----	-----	-----	-----	-----
Balance at December 31, 1997	--	27,814	--	2	--	11,123	11,125
Net earnings	--	--	--	--	--	24,471	24,471
S Corporation distribution	--	--	--	--	--	(7,920)	(7,920)
	-----	-----	-----	-----	-----	-----	-----
Balance at December 31, 1998	--	27,814	--	2	--	27,674	27,676
Net earnings	--	--	--	--	--	24,056	24,056
Proceeds from issuance of common stock in connection with initial public offering	7,000	--	7	26	69,687	--	69,720
Proceeds from issuance of common stock under the employee stock purchase plan	91	--	--	--	261	--	261
S Corporation distribution:							
Cash	--	--	--	--	--	(35,363)	(35,363)
Cross Colours trademark	--	--	--	--	--	(350)	(350)
	-----	-----	-----	-----	-----	-----	-----
Balance at December 31, 1999	7,091	27,814	\$ 7	28	69,948	16,017	86,000
	=====	=====	=====	=====	=====	=====	=====

See accompanying notes to consolidated financial statements.

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SKECHERS U.S.A., INC.

Consolidated Statements of Cash Flows

Three-year period ended December 31, 1999

(In thousands)

	1997	1998	1999
	-----	-----	-----
Cash flows from operating activities:			
Net earnings	\$ 11,023	24,471	24,056
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:			
Depreciation and amortization of property and equipment	1,137	2,843	3,752
Amortization of intangible assets	1,456	148	108
Provision for bad debts and returns	870	1,423	(176)
Loss on disposal of equipment	--	--	903
Gain (loss) on distribution of intangibles	--	190	(118)
Increase in assets:			
Receivables	(12,635)	(17,760)	(17,282)
Inventories	(30,021)	(19,558)	(3,569)
Prepaid expenses and other current assets	(290)	(1,877)	(2,514)
Deferred tax assets	--	--	(2,810)
Other assets	(1,212)	(512)	466
Increase (decrease) in liabilities:			
Accounts payable	27,623	2,132	9,551
Accrued expenses	(83)	4,249	738
	-----	-----	-----
Net cash provided by (used in) operating activities	(2,132)	(4,251)	13,105
	-----	-----	-----
Cash flows used in investing activities:			
Capital expenditures	(6,239)	(9,434)	(10,846)
Intangible assets	(512)	(14)	--
	-----	-----	-----
Net cash used in investing activities	(6,751)	(9,448)	(10,846)
	-----	-----	-----
Cash flows from financing activities:			
Net proceeds from initial public offering of common stock	--	--	69,720
Net proceeds from issuance of common stock	--	--	261
Net proceeds (payments) related to short-term borrowings	10,426	31,486	(23,697)
Proceeds from long-term debt	3,000	581	--
Payments on long-term debt	(25)	(562)	(1,042)
Payments on notes payable to stockholder	--	(1,006)	(12,244)
Distributions paid to stockholders	(3,234)	(7,320)	(35,363)
	-----	-----	-----
Net cash provided by (used in) financing activities	10,167	23,179	(2,365)
	-----	-----	-----
Net increase (decrease) in cash	1,284	9,480	(106)
Cash at beginning of year	178	1,462	10,942
	-----	-----	-----
Cash at end of year	\$ 1,462	10,942	10,836
	=====	=====	=====
Supplemental disclosures of cash flow information:			
Cash paid during the year for:			
Interest	\$ 4,186	8,067	6,782
Income taxes	226	1,416	10,619
	=====	=====	=====

Supplemental disclosures of noncash investing and financing activities:

During 1999, the Company declared a noncash distribution of intangibles of \$350.

During 1998, the Company acquired \$1,372 of property and equipment under capital lease arrangements. In connection with one of these arrangements, the Company received \$581 in cash through a sale leaseback transaction.

See accompanying notes to consolidated financial statements.

## SKECHERS U.S.A., INC.

## Notes to Consolidated Financial Statements

December 31, 1998 and 1999

## (1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

## (a) THE COMPANY

Skechers U.S.A., Inc. (the Company) designs, develops, markets and distributes footwear. The Company also operates retail stores, direct mail and e commerce businesses.

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

## (b) REVENUE RECOGNITION

Revenue is recognized upon shipment of product or at point of sale for retail operations. Allowances for estimated returns and discounts are provided when the related revenue is recorded.

Revenues from royalty agreements are recognized as earned.

## (c) INVENTORIES

Inventories, principally finished goods, are stated at the lower of cost (based on the first-in, first-out method) or market. The Company provides for estimated losses from obsolete or slow-moving inventories.

## (d) INCOME TAXES

The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. 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.

## (e) DEPRECIATION AND AMORTIZATION

Depreciation and amortization of property and equipment is computed using the straight-line method based on the following estimated useful lives:

Furniture, fixtures and equipment	5 years
Leasehold improvements	Useful life or remaining lease term, whichever is shorter

Intangible assets consist of trademarks and are amortized on a straight-line basis over ten years. The accumulated amortization as of December 31, 1998 and 1999 is \$1,088,000 and \$1,196,000, respectively.

## SKECHERS U.S.A., INC.

## Notes to Consolidated Financial Statements

December 31, 1998 and 1999

## (f) LONG-LIVED ASSETS

The Company reports long-lived assets, including intangibles, at amortized cost. As part of an ongoing review of the valuation and amortization of long-lived assets, management assesses the carrying value of assets if facts and circumstances suggest that such assets may be impaired. If this review indicates that the assets will not be recoverable, as determined by a nondiscounted cash flow projections over the remaining amortization period, their carrying value is reduced to estimated fair market value, based on discounted cash flows.

## (g) ADVERTISING COSTS

Advertising costs are expensed as incurred. Advertising expense for the years ended December 31, 1997, 1998 and 1999 approximated \$15,800,000, \$42,200,000 and \$47,400,000, respectively. Prepaid advertising costs at December 31, 1998 and 1999 were \$0 and \$1,800,000, respectively. Prepaid amounts outstanding at December 31, 1999 represent advertising in trade publications which had not run as of December 31, 1999.

## (h) START-UP COSTS

Start-up costs are charged to operations as incurred.

## (i) EARNINGS PER SHARE

Basic earnings per share represents net earnings divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if options to issue common stock were exercised or converted into common stock. The weighted average diluted shares outstanding gives effect to the sale by the Company of those shares of common stock necessary to fund the payment of (i) stockholder distributions paid or declared from January 1, 1998 to June 7, 1999, the S Corporation termination date, in excess of (ii) the S Corporation earnings from January 1, 1998 to December 31, 1998 for both 1997 and 1998, and January 1, 1998 to June 7, 1999 for 1999, based on an initial public offering price of \$11 per share, net of underwriting discounts.

The reconciliation of basic to diluted weighted-average shares is as follows (in thousands):

	1997	1998	1999
	-----	-----	-----
Weighted-average shares used in basic computation	27,814	27,814	31,765
Shares to fund stockholder distributions	1,800	1,800	533
Dilutive effect of stock options	--	996	720
	-----	-----	-----

Weighted-average shares used in diluted computation	29,614 =====	30,610 =====	33,018 =====
---	-----------------	-----------------	-----------------

Options to purchase 1,391,000 and 1,411,000 shares of common stock at prices ranging from \$2.78 to \$6.13 were outstanding at December 31, 1998 and 1999, respectively, but were not included in the computation of diluted earnings per share because the options' exercise price was greater than the average market price of the common shares.

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

(j) USE OF ESTIMATES

Management has made a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

(k) PRODUCT DESIGN AND DEVELOPMENT COSTS

The Company charges all product design and development costs to expense when incurred. Product design and development costs aggregated approximately \$1,800,000, \$2,400,000 and \$2,600,000 during the years ended December 31, 1997, 1998 and 1999, respectively.

(l) COMPREHENSIVE INCOME

The Company reports comprehensive income under Statement of Financial Accounting Standards No. 130, Reporting Comprehensive Income. Except for net earnings, the Company does not have any transactions and other economic events that qualify as comprehensive income as defined under SFAS No. 130. Accordingly, the adoption of SFAS No. 130 did not affect the Company's financial reporting.

(m) FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amount of the Company's financial instruments, which principally include cash, accounts receivable, accounts payable and accrued expenses, approximates fair value due to the relatively short maturity of such instruments.

The fair value of the Company's short-term instruments reflects the fair value based upon current rates available to the Company for similar debt. The fair value of the Company's long-term debt instruments is based on quoted market prices.

(2) PROPERTY AND EQUIPMENT

Property and equipment is summarized as follows (in thousands):

	1998	1999
	-----	-----
Furniture, fixtures and equipment	\$11,849	17,863
Leasehold improvements	8,738	12,392
	-----	-----
Total property and equipment	20,587	30,255
Less accumulated depreciation and amortization	5,391	8,868
	-----	-----
Property and equipment, net	\$15,196	21,387
	=====	=====

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

(3) SHORT-TERM BORROWINGS

The Company has available a secured line of credit, as amended in December 1998, permitting borrowings up to \$120,000,000 based upon eligible accounts receivable and inventories. The agreement expires on December 31, 2002. Borrowings bear interest at the rate of prime (8.5% at December 31, 1999) plus .25% or at LIBOR (6.0% at December 31, 1999) plus 2.75%, as elected by the Company. The agreement provides for the issuance of letters of credit up to a maximum of \$18,000,000, which decreases the amount available for borrowings under the agreement. Outstanding letters of credit at December 31, 1999 were \$4,400,000. Available borrowings under the line of credit at December 31, 1999 was approximately \$39,500,000. The Company pays an unused line of credit fee of .25% annually. The Company is required to maintain certain financial covenants including specified minimum tangible net worth, working capital and leverage ratios as well as limit the payment of dividends if it is in default of any provision of the agreement. The Company was in compliance with these covenants at December 31, 1999.

(4) NOTES PAYABLE TO STOCKHOLDER

Stockholder loans were repaid during 1999. The Company recorded interest expense of approximately \$1,060,000, \$540,000 and \$433,000 related to the stockholder notes during the years ended December 31, 1997, 1998 and 1999, respectively.

(5) LONG-TERM BORROWINGS

Long-term debt at December 31, 1998 and 1999 is as follows (in thousands):

1998	1999
-----	-----

Note payable to bank, due in monthly installments of \$25,000 plus interest at prime (8.5% at December 31, 1999) plus 1%, secured by equipment, due December 2002	\$2,700	2,400
Capital leases, due in aggregate monthly installments of \$64,000, average interest rate of 16.3%, secured by equipment, due through August 2002	1,666	1,168
	-----	-----
	4,366	3,568
Less current installments	816	1,060
	-----	-----
	\$3,550	2,508
	=====	=====

The aggregate maturities of long-term borrowings at December 31, 1999 are as follows:

2000	\$1,060
2001	664
2002	1,844
	-----
	\$3,568
	=====

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

(6) STOCKHOLDERS' EQUITY

(a) STOCK ISSUANCES

Effective as of May 28, 1999, the Company was reincorporated in Delaware. The existing California corporation was merged into a newly formed Delaware corporation and each outstanding share of common stock of the existing California corporation was exchanged, for a share of \$.001 par value Class B common stock of the new Delaware corporation. In addition, pursuant to the reincorporation merger, an approximate 13,907-for-1 common stock split was authorized. The amendment and stock split has been reflected retroactively in the accompanying consolidated financial statements.

The authorized capital stock of the Delaware corporation consists of 100,000,000 shares of Class A common stock, par value \$.001 per share, and 60,000,000 shares of Class B common stock, par value \$.001 per share. The Company has also authorized 10,000,000 shares of preferred stock, \$.001 par value per share.

The Class A common stock and Class B common stock have identical rights other than with respect to voting, conversion and transfer. The Class A common stock is entitled to one vote per share, while the Class B common stock is entitled to ten votes per share on all matters submitted to a vote of stockholders. The shares of Class B common stock are convertible at any time at the option of the holder into shares of Class A common stock on a share-for-share basis. In addition, shares of Class B common stock will be automatically converted into a like number of shares of Class A common stock upon any transfer to any person or entity which is not a permitted transferee.

On June 9, 1999, the Company issued 7,000,000 shares of Class A common stock in an initial public offering and received net proceeds of \$69,720,000.

On February 28, 2000, certain Class B stockholders converted 1,390,710 shares of Class B common stock to Class A common stock.

(b) STOCK OPTION PLAN

In January 1998, the Board of Directors of the Company adopted the 1998 Stock Option, Deferred Stock and Restricted Stock Plan (Stock Option Plan) for the grant of qualified incentive stock options (ISO), stock options not qualified and deferred stock and restricted stock. The exercise price for any option granted may not be less than fair value (110% of fair value for ISOs granted to certain employees). Under the Stock Option Plan, 5,215,154 shares are reserved for issuance. In January 1998, 1,390,715 options to acquire Class A common stock were granted at an exercise price of \$2.78 per share, which was equal to the fair market value. The options vest 25% on June 9, 1999 and 25% each anniversary thereafter over the next three years. In connection with the Company's initial public offering on June 9, 1999, the Company granted 1,209,636 options to acquire Class A common stock at an exercise price of \$11 per share which vest ratably in 20% increments commencing one year from the grant date. During 1999, 84,777 of the \$11 per share options were canceled. The options expire ten years from the date of grant.

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

Shares subject to option under the Stock Option Plan at December 31, 1999 were as follows:

	SHARES	OPTION PRICE
	-----	-----
Outstanding at December 31, 1997	--	\$ --
Granted	1,390,715	2.78
	-----	
Outstanding at December 31, 1998	1,390,715	2.78



Granted	1,209,636	11.00
Canceled	(84,777)	11.00
	-----	
Outstanding at December 31, 1999	2,515,574	2.78 - 11.00
	=====	
Exercisable at December 31, 1999	347,678	2.78
	=====	=====
Options available for grant at December 31, 1999	2,614,803	
	=====	

(c) STOCK PURCHASE PLAN

Effective July 1, 1998, the Company adopted the 1998 Employee Stock Purchase Plan (1998 Stock Purchase Plan). Under terms of the 1998 Stock Purchase Plan, 2,781,415 shares of common stock are reserved for sale to employees at a price no less than 85% of the lower of the fair market value of the Class A common stock at the beginning of the one-year offering period or the end of each of the six-month purchase periods. During 1999, 90,913 shares were issued under the 1998 Stock Purchase Plan for which the Company received \$261,000.

(d) STOCK COMPENSATION

The Company accounts for stock compensation under SFAS No. 123, Accounting for Stock-Based Compensation, and has elected to measure compensation cost under Accounting Principles Board Opinion No. 25 and comply with the pro forma disclosure requirements. Had compensation cost been determined using the fair value at the grant date for awards during 1998 and 1999, consistent with the provisions of SFAS No. 123, the Company's pro forma net earnings (in thousands) and earnings per share would have been reduced to the amounts as indicated below. No stock awards were granted in 1997.

	1998	1999
	-----	-----
Pro forma net earnings	\$ 14,875	19,077
	=====	=====
Pro forma net earnings per share:		
Basic	\$ .53	.60
Diluted	.49	.58
	=====	=====

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The fair value of each option is estimated on the date of grant. The Company used the minimum value method for stock awards prior to its initial public offering and the Black-Scholes option pricing models for stock awards afterwards. The following weighted-average assumptions used for grants were as follows:

	1998	1999
	----	----
Dividend yield	--	--
Expected volatility	--	55%
Risk-free interest rate	5.7%	6.2%
Expected life of option	8	5
	====	====

The weighted-average fair value of options granted during 1998 and 1999 were \$2.78 and \$6.93, respectively.

(7) INCOME TAXES

The pro forma unaudited income tax adjustments represent taxes which would have been reported assuming the Company been subject to federal and state income taxes as a C Corporation. The historical and pro forma provisions for income tax expense were as follows (in thousands):

	1997	1998	1999
	-----	-----	-----
Actual income taxes:			
Federal:			
Current	\$ --	--	8,012
Deferred	--	--	(792)
	-----	-----	-----
Total federal	--	--	7,220
	-----	-----	-----
State:			
Current	390	650	1,480
Deferred	--	--	(65)
	-----	-----	-----
Total state	390	650	1,415
	-----	-----	-----
Total actual income taxes	390	650	8,635
	-----	-----	-----
Pro forma adjustments:			
Federal	3,573	7,864	3,533
State	602	1,534	712
	-----	-----	-----
Total pro forma adjustments	4,175	9,398	4,245
	-----	-----	-----
Total pro forma income taxes	\$ 4,565	10,048	12,880
	=====	=====	=====

## SKECHERS U.S.A., INC.

## Notes to Consolidated Financial Statements

December 31, 1998 and 1999

Pro forma income taxes differs from the statutory tax rate as applied to earnings before income taxes as follows:

	1997	1998	1999
	-----	-----	-----
Expected income tax expense	\$3,880	8,541	11,569
State income tax, net of federal benefit	685	1,507	1,311
	-----	-----	-----
Total provision for pro forma income taxes	\$4,565	10,048	12,880
	=====	=====	=====

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and deferred tax liabilities at December 31, 1999 is presented below:

Deferred tax assets:	
Inventory adjustments	\$ 615,000
State taxes	520,000
Allowances for receivables	1,275,000
Other	808,000
	-----
Total deferred tax assets	3,218,000
	-----
Deferred tax liabilities:	
Depreciation of property and equipment	279,000
Other	129,000
	-----
Total deferred tax liabilities	408,000
	-----
Net deferred tax assets	\$2,810,000
	=====

Management believes it is more likely than not that the results of future operations will generate sufficient taxable income to realize the net deferred tax assets.

Through June 7, 1999, the Company was treated for federal and state

income tax purposes as an S Corporation under Subchapter S of the Internal Revenue Code and comparable state laws. As a result, the earnings of the Company through June 7, 1999 were included in the taxable income of the Company's stockholders for federal and state income tax purposes, and the Company was generally not subject to income tax on such earnings, other than California and other state franchise taxes.

In connection with the Company's initial public offering of its Class A common stock in June 1999, the Company terminated its S Corporation status and became a C Corporation subject to federal and state income taxes. The Company's change of status to a C Corporation resulted in the recording of deferred tax assets amounting to \$1,800,000. This amount is reflected as a reduction of actual income tax expense in the accompanying 1999 consolidated statement of earnings.

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

(8) BUSINESS AND CREDIT CONCENTRATIONS

The Company sells footwear products principally throughout the United States and foreign countries. The footwear industry is impacted by the general economy. Changes in the marketplace may significantly affect management's estimates and the Company's performance. Management performs regular evaluations concerning the ability of customers to satisfy their obligations and provides for estimated doubtful accounts. Domestic accounts receivable amounted to \$45,500,000 and \$57,500,000 before allowance for bad debts and returns at December 31, 1998 and 1999, respectively, which generally do not require collateral from customers. Foreign accounts receivable amounted to \$4,600,000 and \$9,100,000 before allowance for bad debts and returns at December 31, 1998 and 1999, respectively, which generally are collateralized by letters of credit. International net sales amounted to \$27,700,000, \$34,700,000 and \$43,900,000 for the years ended December 31, 1997, 1998 and 1999, respectively. The Company's credit losses for the years ended December 31, 1997, 1998 and 1999 were \$908,000, \$102,000 and \$1,699,000, respectively, and did not significantly differ from management's expectations.

Net sales to customers in the United States exceeded 90% of total net sales for each of the years in the three year period ended December 31, 1999. All long-lived assets of the Company are located in the United States. The Company has no significant assets outside the United States.

During 1997 and 1999, no customer accounted for 10% or more of net sales. During 1998, the Company had one significant customer which accounted for 11.8% of net sales. The Company had one customer which accounted for 12.6% and 10.1% of trade accounts receivable at December 31, 1998 and 1999, respectively.

During 1997, the Company had two manufacturers which accounted for 21.7% and 15.0% of total purchases, respectively. During 1998, the Company had four manufacturers which accounted 15.4%, 14.2%, 12.1% and 10.4% of total purchases, respectively. During 1999, the Company had four manufacturers which accounted 15.5%, 13.4%, 13.3% and 12.3% of total purchases, respectively.

Substantially all of the Company's products are produced in China. The

Company's operations are subject to the customary risks of doing business abroad, including, but not limited to, currency fluctuations, custom duties and related fees, various import controls and other monetary barriers, restrictions on the transfer of funds, labor unrest and strikes and, in certain parts of the world, political instability. The Company believes it has acted to reduce these risks by diversifying manufacturing among various factories. To date, these risk factors have not had a material adverse impact on the Company's operations.

(9) BENEFIT PLAN

The Company has adopted a profit sharing plan covering all employees who are 21 years of age and have completed one year of service. Employees may contribute up to 15.0% of annual compensation. Company contributions to the plan are discretionary and vest over a five-year period. The Company's contributions to the plan amounted to \$93,000, \$242,000 and \$259,000 for the years ended December 31, 1997, 1998 and 1999, respectively.

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

(10) COMMITMENTS AND CONTINGENCIES

(a) LEASES

The Company leases facilities under operating lease agreements expiring through November 2010. The leases are on an all-net basis, whereby the Company pays taxes, maintenance and insurance. The Company also leases certain equipment and automobiles under operating lease agreements expiring at various dates through August 2002. Rent expense for the years ended December 31, 1997, 1998 and 1999 approximated \$3,000,000, \$7,900,000 and \$9,800,000, respectively.

The Company also leases certain property and equipment under capital lease agreements requiring monthly installment payments through August 2002.

Future minimum lease payments under noncancellable leases at December 31, 1999 are as follows (in thousands):

	CAPITAL LEASES -----	OPERATING LEASES -----
Year ending December 31:		
2000	\$ 760	9,954
2001	364	10,125
2002	44	9,837
2003	--	7,728
2004	--	7,035
Thereafter	--	15,186
	-----	-----
	\$ 1,168	59,865

(b) LITIGATION

In December 1999 and January 2000, the Company and two officers/directors were named as defendants in four purported class-action lawsuits. Two of the lawsuits also named the underwriters of the Company's initial public offering as defendants. All of the complaints seek damages and rescission on behalf of a class of persons who purchased securities in, or traceable to, the Company's initial public offering or thereafter on the open market prior to July 6, 1999. As these matters are in the early stages of discovery, neither the Company nor its counsel are able to conclude as to the potential likelihood of an unfavorable outcome. The Company is vigorously defending these complaints and believe their defenses to be meritorious. Accordingly, the Company has not provided for any potential losses associated with these lawsuits.

The Company is involved in other litigation arising from the ordinary course of business. Management does not believe that the disposition of these matters will have a material effect on the Company's financial position or results of operations.

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SKECHERS U.S.A., INC.

Notes to Consolidated Financial Statements

December 31, 1998 and 1999

(c) PURCHASE COMMITMENTS

At December 31, 1999, the Company had purchase commitments of approximately \$104,463,000.

The Company finances production activities in part through the use of interest-bearing open purchase arrangements with certain of its Asian manufacturers. These arrangements currently bear interest at a rate between 1.5% and 2.0% per 30 to 60 day term. The amounts outstanding under these arrangements at December 31, 1998 and 1999 were \$23,500,000 and \$34,900,000, respectively, which are included in accounts payable in the accompanying consolidated financial statements. Interest expense incurred by the Company under these arrangements amounted to \$1,400,000 in 1997, \$2,900,000 in 1998 and \$3,000,000 in 1999.

(11) QUARTERLY SUMMARY OF INFORMATION (UNAUDITED)

Summarized unaudited financial data are as follows (in thousands):

1999	MARCH 31	JUNE 30	SEPTEMBER 30	DECEMBER 31
	-----	-----	-----	-----
Net sales	\$ 95,736	104,582	124,177	100,106
Gross profit	36,698	42,732	52,837	42,341
Pro forma net earnings	2,104	6,248	8,545	2,914
	=====	=====	=====	=====
Pro forma net earnings per share:				
Basic	\$ .08	.21	.25	.08
Diluted	.07	.20	.24	.08

1998	MARCH 31	JUNE 30	SEPTEMBER 30	DECEMBER 31
Net sales	\$ 59,873	87,684	143,045	82,078
Gross profit	22,483	35,997	62,176	33,924
Pro forma net earnings (loss)	651	4,759	13,553	(3,890)
Pro forma net earnings (loss) per share:				
Basic	\$ .02	.17	.49	(.14)
Diluted	.02	.16	.44	(.13)

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SCHEDULE II

SKECHERS U.S.A., INC.

Valuation and Qualifying Accounts

Years ended December 31, 1997, 1998 and 1999

DESCRIPTION	BALANCE AT BEGINNING OF PERIOD	CHARGED TO COSTS AND EXPENSES	DEDUCTIONS AND WRITE-OFFS	BALANCE AT END OF PERIOD
As of December 31, 1997:				
Allowance for obsolescence	\$ 908,000	554,000	(554,000)	908,000
Allowance for doubtful accounts	295,000	1,878,000	(908,000)	1,265,000
Reserve for sales returns and allowances	825,000	5,463,000	(5,563,000)	725,000
As of December 31, 1998:				
Allowance for obsolescence	908,000	64,000	(465,000)	507,000
Allowance for doubtful accounts	1,265,000	702,000	(501,000)	1,466,000
Reserve for sales returns and allowances	725,000	10,840,000	(9,618,000)	1,947,000
As of December 31, 1999:				
Allowance for obsolescence	507,000	134,000	--	641,000
Allowance for doubtful accounts	1,466,000	740,000	(1,699,000)	507,000
Reserve for sales returns and allowances	1,947,000	13,600,000	(12,817,000)	2,730,000

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AMENDMENT NO.1  
TO  
EMPLOYMENT AGREEMENT

THIS AMENDMENT NO. 1 TO EMPLOYMENT AGREEMENT is entered into on February 29, 2000 between Skechers U.S.A., Inc. ("Employer") and Robert Greenberg, an individual ("Employee"), with reference to the following facts:

RECITALS

A. Employer and Employee entered into that certain Employment Agreement (the "Employment Agreement") dated as of June 14, 1999.

B. Employer and Employee intended at the time the Employment Agreement was executed to make payments due thereunder discretionary in that (i) Section 2.2(c) of the Employment Agreement states that the bonus program set forth therein may be replaced with a different program approved by the Board's Compensation Committee and agreed with by Employee and (ii) Section 11.4 permits the amendment, supplement or discharge of the Employment Agreement if in writing signed by both parties.

C. The Board's Compensation Committee has heretofore approved a different bonus program for Employee as set forth herein and Employee has approved such program.

D. Employee and Employer each desire to amend the Employment Agreement effective as of December 31, 1999 to replace the bonus program as set forth in the Employment Agreement.

NOW, THEREFORE, in consideration of the mutual covenants and agreements hereinafter contained, and for other good and valuable consideration, it is hereby agreed by and between the parties hereto as follows:

Terms not defined herein shall have the respective meanings as set forth in the Employment Agreement.

1. COMPENSATION.

Effective as of December 31, 1999, the introductory paragraph to Section 2.2 shall be deleted in its entirety and replaced with the following:

"2.2 Performance-Based Annual Bonus. For each full year during Employee's term as set forth in Section 5, commencing on the Effective Date, Employee shall be eligible to receive a cash bonus based on Employer's achievement of certain financial goals ("Performance-Based Annual Bonus"). For calendar year 2000 (there being no bonus to be paid

to Employee for the calendar year 1999), and until changed by the Board's Compensation Committee, the annual cash bonus award



shall be determined on the basis of Employer's annual return on average equity ("ROE")."

3. Miscellaneous

Section 11 of the Employment Agreement is incorporated herein by reference.

IN WITNESS WHEREOF, this Amendment No. 1, which is made effective as of December 31, 1999, is executed as of the day and year first above written.

"EMPLOYER"

Skechers, U.S.A., Inc.

By: /s/ MICHAEL GREENBERG

-----  
Name: Michael Greenberg  
Title: President

"EMPLOYEE"

/s/ ROBERT GREENBERG

-----  
Robert Greenberg

AMENDMENT NO. 1  
TO  
EMPLOYMENT AGREEMENT

THIS AMENDMENT NO. 1 TO EMPLOYMENT AGREEMENT is entered into on February 29, 2000 between Skechers U.S.A., Inc. ("Employer") and Michael Greenberg, an individual ("Employee"), with reference to the following facts:

RECITALS

A. Employer and Employee entered into that certain Employment Agreement (the "Employment Agreement") dated as of June 14, 1999.

B. Employer and Employee intended at the time the Employment Agreement was executed to make payments due thereunder discretionary in that (i) Section 2.2(c) of the Employment Agreement states that the bonus program set forth therein may be replaced with a different program approved by the Board's Compensation Committee and agreed with by Employee and (ii) Section 11.4 permits the amendment, supplement or discharge of the Employment Agreement if in writing signed by both parties.

C. The Board's Compensation Committee has heretofore approved a different bonus program for Employee as set forth herein and Employee has approved such program.

D. Employee and Employer each desire to amend the Employment Agreement effective as of December 31, 1999 to replace the bonus program as set forth in the Employment Agreement.

NOW, THEREFORE, in consideration of the mutual covenants and agreements hereinafter contained, and for other good and valuable consideration, it is hereby agreed by and between the parties hereto as follows:

Terms not defined herein shall have the respective meanings as set forth in the Employment Agreement.

1. COMPENSATION.

Effective as of December 31, 1999, the introductory paragraph to Section 2.2 shall be deleted in its entirety and replaced with the following:

"2.2 Performance-Based Annual Bonus. For each full year during Employee's term as set forth in Section 5, commencing on the Effective Date, Employee shall be eligible to receive a cash bonus based on Employer's achievement of certain financial goals ("Performance-Based Annual Bonus"), provided, however, that for calendar year 1999,

Employee shall only receive a cash bonus of \$165,000 and not a Performance-Based Annual Bonus. For calendar year 2000, and until changed by the Board's Compensation Committee, the annual cash bonus award shall be determined on the basis of Employer's annual return on average equity ("ROE")."

3. Miscellaneous

Section 11 of the Employment Agreement is incorporated herein by reference.

IN WITNESS WHEREOF, this Amendment No. 1, which is made effective as of December 31, 1999, is executed as of the day and year first above written.

"EMPLOYER"

Skechers, U.S.A., Inc.

By: /s/ DAVID WEINBERG

-----  
Name: David Weinberg  
Title: Executive Vice President and  
Chief Financial Officer

"EMPLOYEE"

/s/ MICHAEL GREENBERG

-----  
Michael Greenberg

AMENDMENT NO. 1  
TO  
EMPLOYMENT AGREEMENT

THIS AMENDMENT NO. 1 TO EMPLOYMENT AGREEMENT is entered into on February 29, 2000 between Skechers U.S.A., Inc. ("Employer") and David Weinberg, an individual ("Employee"), with reference to the following facts:

RECITALS

A. Employer and Employee entered into that certain Employment Agreement (the "Employment Agreement") dated as of June 14, 1999.

B. Employer and Employee intended at the time the Employment Agreement was executed to make payments due thereunder discretionary in that (i) Section 2.2(c) of the Employment Agreement states that the bonus program set forth therein may be replaced with a different program approved by the Board's Compensation Committee and agreed with by Employee and (ii) Section 11.4 permits the amendment, supplement or discharge of the Employment Agreement if in writing signed by both parties.

C. The Board's Compensation Committee has heretofore approved a different bonus program for Employee as set forth herein and Employee has approved such program.

D. Employee and Employer each desire to amend the Employment Agreement effective as of December 31, 1999 to replace the bonus program as set forth in the Employment Agreement.

NOW, THEREFORE, in consideration of the mutual covenants and agreements hereinafter contained, and for other good and valuable consideration, it is hereby agreed by and between the parties hereto as follows:

Terms not defined herein shall have the respective meanings as set forth in the Employment Agreement.

1. COMPENSATION.

Effective as of December 31, 1999, the introductory paragraph to Section 2.2 shall be deleted in its entirety and replaced with the following:

"2.2 Performance-Based Annual Bonus. For each full year during Employee's term as set forth in Section 5, commencing on the Effective Date, Employee shall be eligible to receive a cash bonus based on Employer's achievement of certain financial goals ("Performance-Based Annual Bonus"), provided, however, that for calendar year 1999,

Employee shall only receive a cash bonus of \$150,000 and not a Performance-Based Annual Bonus. For calendar year 2000, and until changed by the Board's Compensation Committee, the annual cash bonus award shall be determined on the basis of Employer's annual return on average equity ("ROE")."

3. Miscellaneous

Section 11 of the Employment Agreement is incorporated herein by reference.

IN WITNESS WHEREOF, this Amendment No. 1, which is made effective as of December 31, 1999, is executed as of the day and year first above written.

"EMPLOYER"

Skechers, U.S.A., Inc.

By: /s/ MICHAEL GREENBERG

-----  
Name: Michael Greenberg  
Title: President

"EMPLOYEE"

/s/ DAVID WEINBERG

-----  
David Weinberg

## INDEMNIFICATION AGREEMENT

THIS INDEMNIFICATION AGREEMENT is made effective as of the 7th day of June, 1999, by and between Skechers U.S.A., Inc., a Delaware corporation (the "Company") and \_\_\_\_\_ ("Indemnitee").

WHEREAS, it is essential to the Company to retain and attract as directors and executive officers the most capable persons available;

WHEREAS, Indemnitee has recently become, or continues to serve as a(n) \_\_\_\_\_ of the Company;

WHEREAS, the Bylaws and the Certificate of Incorporation of the Company require the Company to indemnify its directors and officers to the fullest extent permitted by law and Indemnitee is serving as a director or executive officer of the Company, in part, in reliance on such Bylaws and Certificate of Incorporation; and

WHEREAS, in recognition of Indemnitee's need for substantial protection against personal liability, to maintain Indemnitee's continued service to the Company in an effective manner in reliance on the aforesaid Bylaws and Certificate of Incorporation, in part, to provide Indemnitee with specific contractual assurance that the protection promised by such Bylaws and Certificate of Incorporation will be available to Indemnitee (regardless of, among other things, any amendment to or revocation of such Bylaws and Certificate of Incorporation or any change in the composition of the Company's Board of Directors or any acquisition transaction relating to the Company), the Company desires to provide in this Agreement for the indemnification of and the advance of expenses to Indemnitee to the fullest extent (whether partial or complete) permitted by law, as set forth in this Agreement and, to the extent officers' and directors' liability insurance is maintained by the Company, to provide for continued coverage of Indemnitee under the Company's officers' and directors' liability insurance policies.

NOW, THEREFORE, in consideration of the covenants contained herein and of Indemnitee's continuing service to the Company directly, or at its request, other enterprises, and intending to be legally bound thereby, the parties hereto agree as follows:

## 1. CERTAIN DEFINITIONS

(a) Acquiring Person: shall mean any Person other than: (i) the Company; (ii) any of the Company's Subsidiaries; (iii) any employee benefit plan of the Company or of a Subsidiary of the Company or of a corporation owned directly or indirectly by the stockholders of the Company in substantially the same proportions as their ownership of stock of the Company; (iv) any trustee or other fiduciary holding securities under an employee benefit plan of the Company or of a Subsidiary of the Company or of a corporation owned directly or indirectly by the stockholders of the Company in substantially the same proportions as their ownership of

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stock of the Company; or (v) The Greenberg Family Trust.

(b) Change in Control: shall be deemed to have occurred if: (i) any Acquiring Person is, or becomes the "beneficial owner" (as defined in Rule 13d-3 and 14d-1 under the Securities and Exchange Act of 1934, as amended (the

"Exchange Act")), directly or indirectly, of securities of the Company representing 20% or more of the combined voting power or more of the then outstanding Voting Securities of the Company; or (ii) members of the Incumbent Board cease for any reason to constitute at least a majority of the Board of Directors of the Company; or (iii) a public announcement is made of a tender or exchange offer by an Acquiring Person for 50% or more of the outstanding Voting Securities of the Company, and the Board of Directors of the Company approves or fails to oppose that tender or exchange offer in its statements in Schedule 14D-9 under the Exchange Act; or (iv) the stockholders of the Company approve a merger or consolidation of the Company with any other corporation, partnership or other entity (or, if no such approval is required, the consummation of such a merger or consolidation of the Company), other than a merger or consolidation that would result in the Voting Securities of the Company outstanding immediately prior to the consummation thereof continuing to represent, either by remaining outstanding or by being converted into Voting Securities of the surviving entity or its parent, at least 80% of the total Voting Securities outstanding immediately after that merger or consolidation; or (v) the stockholders of the Company approve a plan of complete liquidation of the Company or an agreement for the sale or disposition by the Company of all or substantially all of the Company's assets (or, if no such approval is required, the consummation of such a liquidation, sale, or disposition in one transaction or series of related transactions) other than a liquidation, sale, or disposition of all or substantially all of the Company's assets in one transaction or a series of related transactions to a corporation owned directly or indirectly by the stockholders of the Company in substantially the same proportions as their ownership of stock of the Company.

(c) Claim: any threatened, pending, or completed action, suit, proceeding or alternative dispute resolution mechanism (including, without limitation, securities laws actions, suits, and proceedings), or any inquiry, hearing or investigation (including discovery), whether conducted by the Company or any other party, that Indemnitee in good faith believes might lead to the institution of any action, suit, proceeding or alternative dispute resolution mechanism whether civil, criminal, administrative, investigative, or other.

(d) Expenses: include attorneys' fees and all other costs, travel expenses, fees of experts, transcript costs, filing fees, witness fees, telephone charges, postage, delivery service fees, expenses and obligations of any nature whatsoever paid or incurred in connection with investigating, defending, being a witness in or participating in (including on appeal), or preparing to defend, be a witness in or participate in any Claim relating to any Indemnifiable Event.

(e) Incumbent Board: individuals, who, as of June 7, 1999 constitute the Board of Directors of the Company and any other individual who becomes a director of the Company after that date and whose election or appointment by the Board of

Directors or nomination for election by the Company's stockholders was approved by a vote of at least a majority of the directors then comprising the Incumbent Board.

(f) Indemnifiable Event: any event or occurrence related to the fact that Indemnitee is or was a director, officer, employee, agent, or fiduciary of the Company, or is or was serving at the request of the Company as a director, officer, employee, trustee, agent, or fiduciary of another corporation, partnership, joint venture, employee benefit plan, trust, or other enterprise, or by reason of anything done or not done by Indemnitee in any such capacity. For purposes of this Agreement, the Company agrees that Indemnitee's service on behalf of or with respect to any Subsidiary of the Company shall be deemed to be at the request of the Company.

(g) Independent Legal Counsel: special, independent counsel selected by Indemnitee and approved by the Company (which approval shall not be unreasonably withheld), and who has not otherwise performed services for the Company or for Indemnitee within the last five years (other than as Independent Legal Counsel under this Agreement or similar agreements). Independent Legal Counsel shall not be any person who, under the applicable standards of professional conduct then prevailing, would have a conflict of interest in representing either the Company or Indemnitee in an action to determine Indemnitee's rights under this Agreement, nor shall Independent Legal Counsel be any person who has been sanctioned or censured for ethical violations of applicable standards of professional conduct.

(h) Person: any person or entity of any nature whatsoever, specifically including an individual, a firm, a company, a corporation, a partnership, a limited liability company, a trust, or other entity. A Person, together with that Person's Affiliates and Associates (as those terms are defined in Rule 12b-2 under the Exchange Act), and any Persons acting as a partnership, limited partnership, joint venture, association, syndicate, or other group (whether or not formally organized), or otherwise acting jointly or in concert or in a coordinated or consciously parallel manner (whether or not pursuant to any express agreement), for the purpose of acquiring, holding, voting, or disposing of securities of the Company with such Person, shall be deemed a single "Person."

(i) Potential Change in Control: shall be deemed to have occurred if (i) the Company enters into an agreement, the consummation of which would result in the occurrence of a Change in Control; (ii) any Person (including the Company) publicly announces an intention to take or to consider taking actions that, if consummated, would constitute a Change in Control; (iii) any Acquiring Person who is or becomes the beneficial owner, directly or indirectly, of securities of the Company representing 10% or more of the combined voting power of the then outstanding Voting Securities of the Company increases its beneficial ownership of such securities by 5% or more over the percentage so owned by that Person on the date of this Agreement; or (iv) the Board of Directors of the Company adopts a resolution to the effect that, for purposes of this Agreement, a Potential Change in Control has occurred.

(j) Reviewing Party: any appropriate person or body consisting of a member

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or members of the Company's Board of Directors or any other person or body appointed by the Board who is not a party to the particular Claim for which Indemnitee is seeking indemnification or Independent Legal Counsel.

(k) Subsidiary: with respect to any Person, any corporation or other entity of which a majority of the voting power of the voting equity securities or equity interest is owned, directly or indirectly, by that Person.

(l) Voting Securities: any securities that vote generally in the election of directors, in the admission of general partners, or in the selection of any other similar governing body.

## 2. BASIC INDEMNIFICATION AND EXPENSE REIMBURSEMENT ARRANGEMENT

(a) If Indemnitee was, is, or becomes a party to or witness or other participant in, or is threatened to be made a party to or witness or other participant in, a Claim by reason of (or arising in part out of) an Indemnifiable Event, the Company shall indemnify Indemnitee to the fullest extent permitted by law as soon as practicable but in any event no later than 30 days after written demand is presented to the Company, against any and all



Expenses, judgments, fines, penalties, or amounts paid in settlement (including all interest, assessments, and other charges paid or payable in connection with or in respect of such Expenses, judgments, fines, penalties, or amounts paid in settlement) of or with respect to that Claim and any federal, state, local or foreign taxes imposed on the Indemnitee as a result of the actual or deemed receipt of any payments under this Agreement (including the creation of the trust referred to in Section 4 hereof). Notwithstanding anything in this Agreement to the contrary and except as provided in Section 5, prior to a Change in Control, Indemnitee shall not be entitled to indemnification pursuant to this Agreement in connection with any Claim initiated by Indemnitee against the Company or any director or officer of the Company unless the Company has joined in or consented to the initiation of such Claim. Notwithstanding the foregoing, the obligations of the Company under Section 2(a) shall be subject to the condition that the Reviewing Party shall not have determined (in a written opinion, in any case in which Independent Legal Counsel referred to in Section 3 hereof is involved) that Indemnitee would not be permitted to be indemnified under applicable law. Nothing contained in this Agreement shall require any determination under this Section 2(a) to be made by the Reviewing Party prior to the disposition or conclusion of the Claim against the Indemnitee; provided, however, that Expense Advances shall continue to be made by the Company pursuant to and to the extent required by the provisions of Section 2(b).

(b) If so requested by Indemnitee, the Company shall pay any and all Expenses incurred by Indemnitee (or, if applicable, reimburse Indemnitee for any and all Expenses incurred by Indemnitee and previously paid by Indemnitee) within five business days after such request (an "Expense Advance"). The Company shall be obligated to make or pay an Expense Advance in advance of the final disposition or conclusion of any Claim. In connection with any request for an Expense Advance, if requested by the Company, Indemnitee or

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Indemnitee's counsel shall submit an affidavit stating that the Expenses incurred were reasonable. Any dispute as to the reasonableness of any Expense shall not delay an Expense Advance by the Company, and the Company agrees that any such dispute shall be resolved only upon the disposition or conclusion of the underlying Claim against the Indemnitee. If, when, and to the extent that the Reviewing Party determines that Indemnitee would not be permitted to be indemnified with respect to a Claim under applicable law, the Company shall be entitled to be reimbursed by Indemnitee and Indemnitee hereby agrees to reimburse the Company without interest (which agreement shall be an unsecured obligation of Indemnitee) for all related Expense Advances theretofore made or paid by the Company; provided, however, that if Indemnitee has commenced legal proceedings in a court of competent jurisdiction to secure a determination that Indemnitee should be indemnified under applicable law, any determination made by the Reviewing Party that Indemnitee would not be permitted to be indemnified under applicable law shall not be binding and Indemnitee shall not be required to reimburse the Company for any Expense Advance, and the Company shall be obligated to continue to make Expense Advances, until a final judicial determination is made with respect thereto (as to which all rights of appeal therefrom have been exhausted or lapsed). If there has not been a Change in Control, the Reviewing Party shall be selected by the Board of Directors of the Company. If there has been a Change in Control, the Reviewing Party shall be advised by or shall be the Independent Legal Counsel referred to in Section 3 hereof, if and as Indemnitee so requests. If there has not been any determination by the Reviewing Party or if the Reviewing Party determines that Indemnitee substantively would not be permitted to be indemnified in whole or in part under applicable law, Indemnitee shall have the right to commence litigation in any court of the States of California or Delaware having subject matter jurisdiction thereof and in which venue is proper seeking an initial determination by the court or challenging any such determination by the Reviewing Party or any aspect thereof, and the Company hereby consents to service of process and to appear in any such proceeding. Any determination by the Reviewing Party otherwise shall be conclusive and binding on the Company and Indemnitee.

### 3. CHANGE IN CONTROL

The Company agrees that, if there is a Change in Control and if Indemnatee requests in writing that Independent Legal Counsel advise the Reviewing Party or be the Reviewing Party, then the Company shall not deny any indemnification payments (and Expense Advances shall continue to be paid by the Company pursuant to Section 2(b)) that Indemnatee requests or demands under this Agreement or any other agreement or law now or hereafter in effect relating to Claims for Indemnifiable Events. The Company further agrees not to request or seek reimbursement from Indemnatee of any related Expense Advances unless, with respect to a denied indemnification payment, Independent Legal Counsel has rendered its written opinion to the Company and Indemnatee that the Company would not be permitted under applicable law to pay Indemnatee such indemnification payment. The Company agrees to pay the reasonable fees of Independent Legal Counsel referred to in this Section 3 and to indemnify fully Independent Legal Counsel against any and all expenses (including attorneys' fees), claims, liabilities, and damages arising out of or relating to this Agreement or Independent Legal Counsel's engagement

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pursuant hereto.

### 4. ESTABLISHMENT OF TRUST

In the event of a Potential Change in Control, the Company shall, upon written request by Indemnatee, create a trust for the benefit of Indemnatee (the "Trust") and from time to time upon written request of Indemnatee the Company shall fund the Trust in an amount sufficient to satisfy any and all Expenses reasonably anticipated at the time of each such request to be incurred in connection with investigating, preparing for, and defending any Claim relating to an Indemnifiable Event, and any and all judgments, fines, penalties, and settlement amounts of any and all Claims relating to an Indemnifiable Event from time to time actually paid or claimed, reasonably anticipated, or proposed to be paid. The amount or amounts to be deposited in the Trust pursuant to the foregoing funding obligation shall be determined by the Reviewing Party, in any situation in which Independent Legal Counsel referred to in Section 3 is involved. The terms of the Trust shall provide that, upon a Change in Control, (i) the Trust shall not be revoked or the principal thereof invaded, without the written consent of Indemnatee; (ii) the trustee of the Trust shall advance, within five business days of a request by Indemnatee, any and all Expenses to Indemnatee (and Indemnatee hereby agrees to reimburse the Trust under the circumstances in which Indemnatee would be required to reimburse the Company for Expense Advances under Section 2(b) of this Agreement); (iii) the Trust shall continue to be funded by the Company in accordance with the funding obligation set forth above; (iv) the trustee of the Trust shall promptly pay to Indemnatee all amounts for which Indemnatee shall be entitled to indemnification pursuant to this Agreement or otherwise; and (v) all unexpended funds in that Trust shall revert to the Company upon a final determination by the Reviewing Party or a court of competent jurisdiction, as the case may be, that Indemnatee has been fully indemnified under the terms of this Agreement. The trustee of the Trust shall be chosen by Indemnatee. Nothing in this Section 4 shall relieve the Company of any of its obligations under this Agreement. All income earned on the assets held in the trust shall be reported as income by the Company for federal, state, local and foreign tax purposes.

### 5. INDEMNIFICATION FOR ADDITIONAL EXPENSES

The Company shall indemnify Indemnatee against any and all costs and expenses (including attorneys' and expert witnesses' fees) and, if requested by Indemnatee, shall (within five business days of that request) advance those costs and expenses to Indemnatee, that are incurred by Indemnatee in connection with any claim asserted against or action brought by Indemnatee for (i) indemnification or advance payment of Expenses by the Company under this Agreement or any other agreement or provision of the Company's Certificate of

Incorporation or Bylaws now or hereafter in effect relating to Claims for Indemnifiable Events and/or (ii) recovery under any directors' and officers' liability insurance policies maintained by the Company, regardless of whether Indemnitee ultimately is determined to be entitled to that indemnification, advance expense payment, or insurance recovery, as the case may be.

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#### 6. PARTIAL INDEMNITY

If Indemnitee is entitled under any provision of this Agreement to indemnification by the Company for some or a portion of the Expenses, judgments, fines, penalties, and amounts paid in settlement of a Claim but not, however, for all of the total amount thereof, the Company shall nevertheless indemnify Indemnitee for the portion thereof to which Indemnitee is entitled. Moreover, notwithstanding any other provision of this Agreement, to the extent that Indemnitee has been successful on the merits or otherwise in defense of any or all Claims relating in whole or in part to an Indemnifiable Event or in defense of any issue or matter therein, including dismissal without prejudice, Indemnitee shall be indemnified against all Expenses incurred in connection therewith.

#### 7. CONTRIBUTION

(a) Contribution Payment: To the extent the indemnification provided for under any provision of this Agreement is determined (in the manner hereinabove provided) not to be permitted under applicable law, then if Indemnitee was, is, or becomes a party to or witness or other participant in, or is threatened to be made a party to or witness or other participant in, a Claim by reason of (or arising in part out of) an Indemnifiable Event, the Company, in lieu of indemnifying Indemnitee, shall contribute to the amount of any and all Expenses, judgments, fines, or penalties assessed against or incurred or paid by Indemnitee on account of that Claim and any and all amounts paid in settlement of that Claim (including all interest, assessments, and other charges paid or payable in connection with or in respect of such Expenses, judgments, fines, penalties, or amounts paid in settlement) for which such indemnification is not permitted ("Contribution Amounts"), in such proportion as is appropriate to reflect the relative fault with respect to the Indemnifiable Event giving rise to the Contribution Amounts of Indemnitee, on the one hand, and of the Company and any and all other parties (including officers and directors of the Company other than Indemnitee) who may be at fault with respect to such Indemnifiable Event (collectively, including the Company, the "Third Parties") on the other hand.

(b) Relative Fault: The relative fault of the Third Parties and the Indemnitee shall be determined (i) by reference to the relative fault of Indemnitee as determined by the court or other governmental agency assessing the Contribution Amount, or (ii) to the extent such court or other governmental agency does not apportion relative fault, by the Reviewing Party (which shall include Independent Legal Counsel) after giving effect to, among other things, the relative intent, knowledge, access to information, and opportunity to prevent or correct the applicable Indemnifiable Event and other relevant equitable considerations of each party. The Company and Indemnitee agree that it would not be just and equitable if contribution pursuant to this Section 7 were determined by pro rata allocation or by any other method of allocation which does take account of the equitable considerations referred to in this Section 7(b).

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## 8. BURDEN OF PROOF

It shall be a defense to any action brought by the Indemnitee against the Company to enforce this Agreement (other than an action brought to enforce a claim for expenses incurred in defending a Claim in advance of its final disposition where the required undertaking has been tendered by the Company) that the Indemnitee has not met the standards of conduct that make it permissible under the Delaware General Corporation Law for the Company to indemnify the Indemnitee for the amount claimed. In connection with any determination by the Reviewing Party or otherwise as to whether Indemnitee is entitled to be indemnified under any provision of this Agreement or to receive contribution pursuant to Section 7 of this Agreement, the burden of proof shall be on the Company to establish that Indemnitee is not so entitled.

## 9. NO PRESUMPTION

For purposes of this Agreement, the termination of any claim, action, suit, or proceeding, by judgment, order, settlement (whether with or without court approval), or conviction, or upon a plea of nolo contendere, or its equivalent, shall not create a presumption that Indemnitee did not meet any particular standard of conduct or have any particular belief or that a court has determined that indemnification is not permitted by applicable law.

## 10. NON-EXCLUSIVITY

The rights of Indemnitee hereunder shall be in addition to any other rights Indemnitee may have under the Company's Certificate of Incorporation or Bylaws, the Delaware General Corporation Law or otherwise. To the extent that a change in the Delaware General Corporation Law (whether by statute or judicial decision) permits greater indemnification by agreement than would be afforded currently under the Company's Certificate of Incorporation or Bylaws and this Agreement, it is the intent of the parties hereto that Indemnitee shall enjoy by this Agreement the greater benefits so afforded by that change.

## 11. NO CONSTRUCTION AS EMPLOYMENT AGREEMENT

Nothing contained herein shall be construed as giving Indemnitee any right to be retained in the employ of the Company or any of its Subsidiaries.

## 12. LIABILITY INSURANCE

Except as otherwise agreed to by the Company and Indemnitee in a written agreement, to the extent the Company maintains an insurance policy or policies providing directors' and officers' liability insurance, Indemnitee shall be covered by that policy or those policies, in accordance with its or their terms, to the maximum extent of the coverage available for any Company director or officer.

## 13. PERIOD OF LIMITATIONS

No legal action shall be brought and no cause of action shall be asserted by or on behalf of the Company or any affiliate of the Company against Indemnitee or Indemnitee's spouse, heirs, executors, or personal or legal representatives after the expiration of three years from the date of accrual of that cause of action, and any claim or cause of action of the Company or its

affiliate shall be extinguished and deemed released unless asserted by the timely filing of a legal action within that three-year period; provided, however, that, if any shorter period of limitations is otherwise applicable to any such cause of action, the shorter period shall govern.

14. AMENDMENTS

No supplement, modification, or amendment of this Agreement shall be binding unless executed in writing by both of the parties hereto. No waiver of any of the provisions of this Agreement shall be deemed or shall constitute a waiver of any other provisions hereof (whether or not similar) nor shall that waiver constitute a continuing waiver.

15. SUBROGATION

In the event of payment under this Agreement, the Company shall be subrogated to the extent of that payment to all of the rights of recovery of Indemnitee, who shall execute all papers required and shall do everything that may be necessary to secure those rights, including the execution of the documents necessary to enable the Company effectively to bring suit to enforce those rights.

16. NO DUPLICATION OF PAYMENTS

The Company shall not be liable under this Agreement to make any payment in connection with any claim made against Indemnitee to the extent Indemnitee has otherwise actually received payment (under any insurance policy, provision of the Company's charter or Bylaws or otherwise) of the amounts otherwise indemnifiable hereunder.

17. BINDING EFFECT; MERGER

This Agreement shall be binding upon and inure to the benefit of and be enforceable by the parties hereto and their respective successors, assigns (including any direct or indirect successor by purchase, merger, consolidation, or otherwise to all or substantially all of the business or assets of the Company), spouses, heirs, and personal and legal representatives. The Company shall require and cause any successor (whether direct or indirect by purchase, merger, consolidation or otherwise) to all, substantially all, or by written agreement in form and substance satisfactory to Indemnitee, expressly to assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform if no such succession had taken place. This Agreement shall continue in effect regardless of whether

Indemnitee continues to serve as an officer or director of the Company or another enterprise at the Company's request.

18. SEVERABILITY

If any provision of this Agreement is held to be illegal, invalid, or unenforceable under present or future laws effective during the term hereof, that provision shall be fully severable; this Agreement shall be construed and enforced as if that illegal, invalid, or unenforceable provision had never comprised a part hereof; and the remaining provisions shall remain in full force and effect and shall not be affected by the illegal, invalid, or unenforceable provision or by its severance from this Agreement. Furthermore, in lieu of that illegal, invalid, or unenforceable provision, there shall be added automatically as a part of this Agreement a provision as similar in terms to the illegal, invalid, or unenforceable provision as may be possible and be legal, valid, and enforceable.

19. GOVERNING LAW

This Agreement shall be governed by and construed and enforced in accordance with the laws of the State of Delaware applicable to contracts made and to be performed in that state without giving effect to the principles of conflicts of laws or choice of laws.

20. CONSTRUCTION

The headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. Pronouns shall be construed to include the masculine, feminine, neuter, singular and plural as the context requires.

21. NOTICES

Whenever this Agreement requires or permits notice to be given by one party to the other, such notice must be in writing to be effective and shall be deemed delivered and received by the party to whom it is sent upon actual receipt (by any means) of such notice. Receipt of a notice by any officer of the Company shall be deemed receipt of such notice by the Company.

22. COUNTERPARTS

This Agreement may be executed in any number of counterparts, each of which shall be deemed an original, but in making proof hereof it shall not be necessary to produce or account for more than one such counterpart.

IN WITNESS WHEREOF, the undersigned has executed this agreement as of the date first written above.

SKECHERS U.S.A., INC.  
a Delaware corporation

By: /s/ Robert Greenberg

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Robert Greenberg  
Chief Executive Officer

INDEMNITEE:

By: \_\_\_\_\_

LIST OF REGISTRANT'S DIRECTORS AND EXECUTIVE OFFICERS  
WHO ENTERED INTO INDEMNIFICATION AGREEMENT  
REFERENCED IN EXHIBIT 10.6 WITH THE REGISTRANT

1. Robert Greenberg
2. Michael Greenberg
3. David Weinberg
4. Philip Paccione
5. John Quinn
6. Richard Siskind

## INDUSTRIAL/COMMERCIAL SINGLE-TENANT LEASE NET

## 1. BASIC PROVISIONS ("BASIC PROVISIONS").

## 1.1. PARTIES:

This Lease ("Lease"), dated for reference purposes only, November 15, 1999, is made by and between - CHAMPAGNE BUILDING GROUP, LP, a California limited partnership ("LESSOR") or ("LANDLORD") and SKECHERS USA, INC., a Delaware Corporation ("LESSEE" or "TENANT"), (collectively the "PARTIES," or individually a "PARTY").

## 1.2. PREMISES:

That certain real property, including the "BASE BUILDING" as defined in the Work Letter attached hereto as Exhibit A to be provided by Lessor under the terms of this Lease, plus those improvements to be separately constructed by Tenant pursuant to the Work Letter (the "TENANT IMPROVEMENTS") together with the land described in the legal description attached hereto as "LEGAL DESCRIPTION" and commonly known as 1670 S. Champagne Avenue, Ontario located in the County of San Bernardino, State of California and generally described as an approximate 263,670 square foot free standing distribution building (all of such real property, including, without limitation, such land, all improvements upon such land, the Base Building and Tenant Improvements are collectively referred to herein as the "PREMISES"). (See also Paragraph 2)

## 1.3. TERM:

Seven (7) years and Zero (0) months ("ORIGINAL TERM") commencing upon Substantial Completion (as defined in the Addendum) ("COMMENCEMENT DATE") and ending Seven years after the Commencement Date ("EXPIRATION DATE"). Landlord agrees that Substantial Completion, and therefore, the Commencement Date, shall be not later than May 15, 2000 (the "SCHEDULED COMMENCEMENT DATE") subject to Force Majeure Delays (as defined in the Addendum) (See also Paragraph 3)

## 1.4. EARLY POSSESSION:

March 15, 2000 or as agreed subject to Force Majeure Delays ("EARLY POSSESSION DATE"). (See also Paragraphs 3.2 and 3.3)

## 1.5. BASE RENT:

\$85,693.00 per month ("BASE RENT"), payable on the first day of each month commencing the first day following Substantial Completion (See also Paragraph 4)

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If this box is checked, there are provisions in this Lease for the Base Rent to be adjusted (see Addendum Paragraph 50)

## 1.6. BASE RENT PAID UPON EXECUTION:

\$85,693.00 as Base Rent for the period: first month's rent

## 1.7. SECURITY DEPOSIT:



\$85,693.00 ("Security Deposit") in addition to the Base Rent Paid Upon Execution. (See also Paragraph 5)

1.8. AGREED USE:

Warehousing, distribution, office and showroom and uses reasonably related to the foregoing (See also Paragraph 6)

1.9. INSURING PARTY:

Lessor is the "Insuring Party" unless otherwise stated herein. (See also Paragraph 8)

1.10. REAL ESTATE BROKERS:

(See also Paragraph 15)

(a) Representation: The following real estate brokers (collectively, the "Brokers") and brokerage relationships exist in this transaction (check applicable boxes):

The Seeley Company represents Lessor exclusively ("Lessor's Broker");

CB Richard Ellis represents Lessee exclusively ("Lessee's Broker")

(b) Payment to Brokers: Upon execution and delivery of this Lease by both Parties, Lessor shall pay to the Broker the fee agreed to in their separate written agreement

1.11. GUARANTOR.

The obligations of the Lessee under this Lease are to be guaranteed by N/A ("Guarantor"). (See also Paragraph 37)

1.12. ADDENDA AND EXHIBITS.

Attached hereto is an Addendum or Addenda consisting of Paragraphs 50 through 65, the Legal Description, and Exhibits A (Work Letter) and B (Protected Lessee Owned Alterations) all of which constitute a part of this Lease.

2. PREMISES.

2.1. LETTING.

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Lessor hereby leases to Lessee, and Lessee hereby leases from Lessor, the Premises, for the term, at the rental, and upon all of the terms, covenants and conditions set forth in this Lease. Unless otherwise provided herein, any statement of size set forth in this Lease, or that may have been used in calculating rental, is an approximation which the Parties agree is reasonable and the rental based thereon is not subject to revision whether or not the actual size is more or less.

2.2. CONDITION.

Lessor shall deliver the Base Building (as defined in the Work Letter, and sometimes referred to herein as the "Building") to Lessee broom clean and free of debris (except dirt and debris caused by Tenant) on the Commencement Date, and, so long as the required service contracts described in Paragraph 7.1 (b) below are obtained by Lessee within thirty (30) days following the Commencement Date, Lessor warrants that the Base Building, including, without limitation, existing electrical,

plumbing, fire sprinkler, lighting, heating, ventilating and air conditioning systems ("HVAC"), loading doors, if any, and all other such elements in the Premises, other than those constructed by Lessee, shall be in good operating condition on said date and shall be free of material defects. Notwithstanding Lessee's failure to obtain such required service contracts within thirty (30) days following the Commencement Date, the Lessor warranty described in the foregoing sentence shall nevertheless continue so long as Lessee has obtained all of such required service contracts within ten (10) days following notice from Lessor subsequent to such thirty (30) day period to the effect that Lessee has not obtained such required service contracts (the "Service Contract Deficiency Notice") and must do so within ten (10) days of such Service Contract Deficiency Notice or Lessor will be relieved of the Lessor warranty described in the first sentence of Paragraph 2.2 of the Lease. If a non-compliance with said warranty exists as of the Commencement Date, Lessor shall, as Lessor's sole obligation with respect to such matter, except as otherwise provided in this Lease, promptly after receipt of written notice from Lessee setting forth with specificity the nature and extent of such non-compliance, rectify same at Lessor's expense. If, after the Commencement Date, Lessee does not give Lessor written notice of any non-compliance with this warranty within: (i) five (5) years as to the roof and the structural portion of the roof, (ii) two (2) years as to the slab and concrete walls, and (iii) one (1) year as to the remaining systems and other elements of the Building, correction of such non-compliance shall be the obligation of Lessee at Lessee's sole cost and expense; provided, however, that Lessee's sole obligation with respect to the items specified in subsections (i)(iii) of this sentence shall not commence unless and until Lessor has given to Lessee notice that as to such applicable subsection Lessor's obligations are ending or have ended and Lessee's obligations are beginning or have begun. Lessor's obligations with respect to any warranties given to Lessee pursuant to this Section 2.2 are conditioned upon the following: (a) Lessee shall have given notice to Lessor of any claims on such warranties promptly and in no event not later than twenty (20) days after the discovery of the condition giving rise to such claim and (b) except in connection with an emergency that threatens property or safety, if Lessee or any person other than a person selected by Lessor repairs or otherwise attempts to correct an conditions giving rise to the claim, Lessor shall be relieved of the warranty obligations related to such condition repaired or corrected by such other person.

### 2.3. COMPLIANCE.

Lessor warrants that the improvements on the Premises comply with all applicable laws, covenants or restrictions of record, building codes, regulations and ordinances ("Applicable Requirements") in effect on the Commencement Date. Said warranty does not apply to the use to which Lessee will put the Premises or to any Alterations or Utility Installations (as defined in Paragraph 7.3(a)) made or to be made by Lessee. NOTE: Lessee is responsible for determining whether or not the zoning is appropriate for Lessee's intended use, and acknowledges that past uses of the Premises may no longer be allowed. If the Premises do not comply with said warranty, Lessor shall, except as otherwise provided, promptly after receipt of written notice from Lessee setting forth with specificity the nature and extent of such non-compliance, rectify the same at Lessor's expense. If Lessee does not give Lessor written notice of a non-compliance with this warranty within six (6) months following the Commencement Date, correction of that non-compliance shall be the obligation of Lessee at Lessee's sole cost and expense. If the Applicable Requirements are hereafter changed (as opposed to being in existence at the Commencement Date) so as to require during the term of this Lease the construction of an addition to or an

alteration of the Building, the remediation of any Hazardous Substance, or the reinforcement or other physical modification of the Building ("Capital Expenditure"), Lessor and Lessee shall allocate the cost of such work as follows:

- (a) Subject to Paragraph 2.3(c) below, if such Capital Expenditures are required as a result of the specific and unique use of the Premises by Lessee as compared with uses by tenants in general, Lessee shall be fully responsible for the cost thereof, provided, however, that if such Capital Expenditure is required during the last two (2) years of this Lease and the cost thereof exceeds six (6) months' Base Rent, Lessee may instead terminate this Lease unless Lessor notifies Lessee, in writing, within ten (10) days after receipt of Lessee's termination notice that Lessor has elected to pay the difference between the actual cost thereof and the amount equal to six (6) months' Base Rent. If Lessee elects termination, Lessee shall immediately cease the use of the Premises which requires such Capital Expenditure and deliver to Lessor written notice specifying a termination date at least ninety (90) days thereafter. Such termination date shall, however, in no event be earlier than the last day that Lessee could legally utilize the Premises without commencing such Capital Expenditure.
- (b) If such Capital Expenditure is not the result of the specific and unique use of the Premises by Lessee (such as, governmentally mandated seismic modifications), then Lessor and Lessee shall allocate the obligation to pay for such costs pursuant to the provisions of Paragraph 7.1 (c); provided, however, that if such Capital Expenditure is required during the last two years of this Lease or if Lessor reasonably determines that it is not economically feasible to pay its share thereof, Lessor shall have the option to terminate this Lease upon ninety (90) days prior written notice to Lessee unless Lessee notifies Lessor, in writing, within ten (10) days after receipt of Lessor's termination notice that Lessee will pay for such Capital Expenditure. If Lessor does not elect to terminate, and fails to tender its share of any such Capital Expenditure, Lessee may advance such funds and deduct same, with interest, from Rent until Lessors share of such costs have been fully paid. If Lessee is unable to finance Lessor's share, or if the balance of the Rent due and payable for the remainder of this Lease is not sufficient to fully reimburse Lessee on

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an offset basis, Lessee shall have the right to terminate this Lease upon thirty (30) days written notice to Lessor.

- (c) Notwithstanding the above, the provisions concerning Capital Expenditures are intended to apply only to non-voluntary, unexpected, and new Applicable Requirements. If the Capital Expenditures are instead triggered by Lessee as a result of an actual or proposed change in use, change in intensity of use, or modification to the Premises then, and in that event, Lessee shall be fully responsible for the cost thereof, and Lessee shall not have any right to terminate this Lease.

#### 2.4. ACKNOWLEDGEMENTS.

[intentionally omitted]

#### 2.5. LESSEE AS PRIOR OWNER/OCCUPANT.

[intentionally omitted]

3. TERM.

3.1. TERM.

The Commencement Date, Expiration Date and Original Term of this Lease are as specified in Paragraph 1.3.

3.2. EARLY POSSESSION.

If Lessee totally or partially occupies the Premises prior to the Commencement Date, the obligation to pay Base Rent shall be abated for the period of such early possession. All other terms of this Lease (including, but not limited to, the obligations to pay Real Property Taxes and insurance premiums and to maintain the Premises) shall, however, be in effect during such period. Any such early possession shall not affect the Expiration Date.

3.3. DELAY IN POSSESSION.

(See Addendum Paragraph 61)

3.4. LESSEE COMPLIANCE.

Lessor shall not be required to tender possession of the Premises to Lessee until Lessee complies with its obligation to provide evidence of insurance (Paragraph 8.5). Pending delivery of such evidence, Lessee shall be required to perform all of its obligations under this Lease from and after the Commencement Date, including the payment of Rent, notwithstanding Lessor's election to withhold possession pending receipt of such evidence of insurance. Further, if Lessee is required to perform any other conditions prior to or concurrent with the Early Possession Date, the Early Possession Date shall occur but Lessor may elect to withhold possession until such conditions are satisfied.

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4. RENT.

4.1. RENT DEFINED.

All monetary obligations of Lessee to Lessor under the terms of this Lease (except for the Security Deposit) are deemed to be rent ("RENT").

4.2. PAYMENT.

Lessee shall cause payment of Rent to be received by Lessor in lawful money of the United States, without offset or deduction (except as specifically permitted in this Lease), on or before the day on which it is due. Rent for any period during the term hereof which is for less than one (1) full calendar month shall be prorated based upon the actual number of days of said month. Payment of Rent shall be made to Lessor at its address stated herein or to such other persons or place as Lessor may from time to time designate in writing. Acceptance of a payment which is less than the amount then due shall not be a waiver of Lessor's rights to the balance of such Rent, regardless of Lessors endorsement of any check so stating.

5. SECURITY DEPOSIT.

Lessee shall deposit with Lessor upon execution hereof the Security Deposit as security for Lessee's faithful performance of its obligations under this Lease. If Lessee fails to pay Rent, or otherwise Defaults under this Lease, Lessor may use, apply or retain all or any portion of said Security Deposit for the payment of any amount due Lessor or to reimburse or compensate Lessor for any liability, expense, loss or

damage which Lessor may suffer or incur by reason thereof. If Lessor uses or applies all or any portion of said Security Deposit, Lessee shall within ten (10) days after written request therefor deposit monies with Lessor sufficient to restore said Security Deposit to the full amount required by this Lease. If the Base Rent increases during the term of this Lease, Lessee shall, upon written request from Lessor, deposit additional monies with Lessor so that the total amount of the Security Deposit shall at all times bear the same proportion to the increased Base Rent as the initial Security Deposit bore to the initial Base Rent. Should the Agreed Use be amended to accommodate a material change in the business of Lessee or to accommodate a sublessee or assignee, Lessor shall have the right to increase the Security Deposit to the extent necessary, in Lessor's reasonable judgment, to account for any increased wear and tear that the Premises may suffer as a result thereof. If a change in control of Lessee occurs during this Lease and following such change the financial condition of Lessee is, in Lessor's reasonable judgment, significantly reduced, Lessee shall deposit such additional monies with Lessor as shall be sufficient to cause the Security Deposit to be at a commercially reasonable level based on said change in financial condition. Lessor shall not be required to keep the Security Deposit separate from its general accounts. Within fourteen (14) days after the expiration or termination of this Lease, if Lessor elects to apply the Security Deposit only to unpaid Rent, and otherwise within thirty (30) days after the Premises have been vacated pursuant to Paragraph 7.4(c) below, Lessor shall return that portion of the Security Deposit not used or applied by Lessor. No part of the Security Deposit shall be considered to be held in trust, to bear interest (except as hereinafter set forth)

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or to be prepayment for any monies to be paid by Lessee under this Lease. Upon the return of the unused amounts of the Security Deposit, Lessor shall pay to Lessee an amount equal to simple (not compounded) interest on the portions of the Security Deposit unused from time to time during the Term. Lessor shall make such interest calculations on a monthly basis (using a 30 day month) using a simple interest rate of five (5%).

## 6. USE.

### 6.1. USE.

Lessee shall use and occupy the Premises only for the Agreed Use, or any other legal use which is reasonably comparable thereto, and for no other purpose. Lessee shall not use or permit the use of the Premises in a manner that is unlawful, creates damage, waste or a nuisance, or that disturbs owners and/or occupants of, or causes damage to neighboring properties. Lessor shall not unreasonably withhold or delay its consent to any written request for a modification of the Agreed Use, so long as the same will not impair the structural integrity of the improvements on the Premises or the mechanical or electrical systems therein, is not significantly more burdensome to the Premises. If Lessor elects to withhold consent, Lessor shall within five (5) business days after such request give written notification of same, which notice shall include an explanation of Lessor's objections to the change in use.

### 6.2. HAZARDOUS SUBSTANCES.

(a) REPORTABLE USES REQUIRE CONSENT. The term "HAZARDOUS SUBSTANCE" as used in this Lease shall mean any product, substance, or waste whose presence, use, manufacture, disposal, transportation, or release, either by itself or in combination with other materials expected to be on the Premises, is either: (i) potentially injurious to the public health, safety or welfare, the environment or the Premises,

(ii) regulated or monitored by any governmental authority, or (iii) a basis for potential liability of Lessor to any governmental agency or third party under any applicable statute or common law theory. Hazardous Substances shall include, but not be limited to, hydrocarbons, petroleum, gasoline, and/or crude oil or any products, by-products or fractions thereof. Lessee shall not engage in any activity in or on the Premises which constitutes a Reportable Use of Hazardous Substances without the express prior written consent of Lessor and timely compliance (at Lessee's expense) with all Applicable Requirements. "REPORTABLE USE" shall mean (1) the installation or use of any above or below ground storage tank, (2) the generation, possession, storage, use, transportation, or disposal of a Hazardous Substance that requires a permit from, or with respect to which a report, notice, registration or business plan is required to be filed with, any governmental authority, and/or (3) the presence at the Premises of a Hazardous Substance with respect to which any Applicable Requirements requires that a notice be given to persons entering or occupying the Premises or neighboring properties. Notwithstanding the foregoing, Lessee may use any ordinary and customary materials reasonably required to be used in the normal course of the Agreed Use, so long as such use is in compliance with, all Applicable Requirements, is not a Reportable Use, and does not expose the Premises or neighboring property to any meaningful risk of contamination or damage or expose Lessor to any liability therefor. In addition, Lessor may condition its consent to any Reportable Use upon receiving such additional assurances as Lessor reasonably deems necessary to protect

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itself, the public, the Premises and/or the environment against damage, contamination, injury and/or liability, including, but not limited to, the installation (and removal on or before Lease expiration or termination) of protective modifications (such as concrete encasements) and/or increasing the Security Deposit.

(b) DUTY TO INFORM LESSOR. If Lessee knows, or has reasonable cause to believe, that a Hazardous Substance has come to be located in, on, under or about the Premises, other than as previously consented to by Lessor, Lessee shall immediately give written notice of such fact to Lessor, and provide Lessor with a copy of any report, notice, claim or other documentation which it has concerning the presence of such Hazardous Substance.

(c) LESSEE REMEDIATION. Lessee shall not cause or permit any Hazardous Substance to be spilled or released in, on, under, or about the Premises (including through the plumbing or sanitary sewer system) and shall promptly, at Lessee's expense, take all investigatory and/or remedial action reasonably recommended, whether or not formally ordered or required, for the cleanup of any contamination of, and for the maintenance, security and/or monitoring of the Premises or neighboring properties, that was caused or materially contributed to by Lessee, or pertaining to or involving any Hazardous Substance brought onto the Premises during the term of this Lease, by or for Lessee, or any third party. Notwithstanding the foregoing, Lessee shall have no liability under this Lease with respect to underground migration of any Hazardous Substance under the Premises from adjacent properties unless such adjacent properties are owned or occupied by Lessee, and then only to the extent caused by Lessee.

(d) LESSEE INDEMNIFICATION. Lessee shall indemnify, defend and hold Lessor, its agents, employees, lenders and ground lessor, if any, harmless from and against any and all loss of rents and/or damages, liabilities, judgments, claims, expenses, penalties, and attorneys' and consultants' fees arising out of or involving any Hazardous Substance brought onto the Premises by or for Lessee, or any third party

(provided, however, that Lessor shall have no liability under this Lease with respect to underground migration of any Hazardous Substance under the Premises from adjacent properties occurring after the Commencement Date). Lessee's obligations shall include, but not be limited to, the effects of any contamination or injury to person, property or the environment created or suffered by Lessee, and the cost of investigation, removal, remediation, restoration and/or abatement, and shall survive the expiration or termination of this Lease. No termination, cancellation or release agreement entered into by Lessor and Lessee shall release Lessee from its obligations under this Lease with respect to Hazardous Substances, unless specifically so agreed by Lessor in writing at the time of such agreement

(e) LESSOR INDEMNIFICATION. Lessor and its successors and assigns shall indemnify, defend, reimburse and hold Lessee, its employees and lenders, harmless from and against any and all damages, liabilities, judgments, claims, expenses, penalties, and attorneys' and consultants' fees and all environmental damages, including the cost of remediation, arising out of or involving any Hazardous Substances on the Premises prior to the Commencement Date or which are caused by the gross negligence or willful misconduct of Lessor, its agents or employees. Lessor's obligations, as and when required by the Applicable Requirements, shall include, but not be limited to, the cost of investigation, removal, remediation, restoration and/or abatement, and shall survive the expiration or termination of this Lease. No termination, cancellation or release agreement entered into by Lessor and Lessee shall release Lessor from its obligations under this Lease with respect to Hazardous Substances, unless specifically so agreed by Lessee in writing at the time of such agreement.

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(f) INVESTIGATIONS AND REMEDIATIONS. Lessor shall retain the responsibility and pay for any investigations or remediation measures required by governmental entities having jurisdiction with respect to the existence of Hazardous Substances on the Premises prior to the Commencement Date, unless such remediation measure is required as a result of Lessee's use (including "Alterations", as defined in Paragraph 7.3(a) below) of the Premises, in which event Lessee shall be responsible for such payment. Lessee shall cooperate fully in any such activities at the request of Lessor, including allowing Lessor and Lessor's agents to have reasonable access to the Premises at reasonable times in order to carry out Lessor's investigative and remedial responsibilities.

(g) LESSOR TERMINATION OPTION. If a Hazardous Substance Condition occurs during the term of this Lease, unless Lessee is legally responsible therefor (in which case Lessee shall make the investigation and remediation thereof required by the Applicable Requirements and this Lease shall continue in full force and effect, but subject to Lessor's rights under Paragraph 6.2(d) and Paragraph 13), Lessor may, at Lessor's option, either (i) investigate and remediate such Hazardous Substance Condition, if required, as soon as reasonably possible at Lessors expense, in which event this Lease shall continue in full force and effect, or (ii) if the estimated cost to remediate such condition exceeds twelve (12) times the then monthly Base Rent or \$100,000, whichever is greater, give written notice to Lessee, within thirty (30) days after receipt by Lessor of knowledge of the occurrence of such Hazardous Substance Condition, of Lessor's desire to terminate this Lease as of the date sixty (60) days following the date of such notice. In the event Lessor elects to give a termination notice, Lessee may, within ten (10) days thereafter, give written notice to Lessor of Lessee's commitment to pay the amount by which the cost of the remediation of such Hazardous Substance Condition exceeds an amount equal to twelve (12) times the then monthly Base Rent or \$100,000,

whichever is greater, Lessee shall provide Lessor with said funds or satisfactory assurance thereof within thirty (30) days following such commitment. In such event, this Lease shall continue in full force and effect, and Lessor shall proceed to make such remediation as soon as reasonably possible after the required funds are available. If Lessee does not give such notice and provide the required funds or assurance thereof within the time provided, this Lease shall terminate as of the date specified in Lessor's notice of termination.

#### 6.3. LESSEE'S COMPLIANCE WITH APPLICABLE REQUIREMENTS.

Except as otherwise provided in this Lease (and, in particular, Paragraphs 2.2 and 2.3 hereof), Lessee shall, at Lessee's sole expense, fully, diligently and in a timely manner, materially comply with all Applicable Requirements, and the requirements of any applicable fire insurance underwriter or rating bureau, without regard to whether said requirements are now in effect or become effective after the Early Possession Date. Lessee shall, within ten (10) days after receipt of Lessor's written request, provide Lessor with copies of all permits and other documents, and other information evidencing Lessee's compliance with any Applicable Requirements specified by Lessor, and shall immediately upon receipt, notify Lessor in writing (with copies of any documents involved) of any threatened or actual claim, notice, citation, warning, complaint or report pertaining to or involving the failure of Lessee or the Premises to comply with any Applicable Requirements.

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#### 6.4. INSPECTION; COMPLIANCE.

Lessor and Lessor's "Lender" (as defined in Paragraph 30 below) and consultants shall have the right to enter into Premises at any time, in the case of an emergency, and otherwise at reasonable times, for the purpose of inspecting the condition of the Premises and for verifying compliance by Lessee with this Lease. The cost of any such inspections shall be paid by Lessor, unless a violation of Applicable Requirements, or a contamination is found to exist or be imminent, or the inspection is requested or ordered by a governmental authority. In such case, Lessee shall upon request reimburse Lessor for the cost of such inspections, so long as such inspection is reasonably related to the violation or contamination.

#### 7. MAINTENANCE; REPAIRS, UTILITY INSTALLATIONS; TRADE FIXTURES AND ALTERATIONS.

##### 7.1. LESSEE'S OBLIGATIONS.

(a) IN GENERAL. Subject to the provisions of Paragraph 2.2 (Condition), 2.3 (Compliance), 6.3 (Lessee's Compliance with Applicable Requirements), 7.2 (Lessor's Obligations), 9 (Damage or Destruction), 14 (Condemnation), and the Work Letter (which provisions shall control over any conflicting provisions in this Paragraph 7.1 (a)), Lessee shall, at Lessee's sole expense, keep the Premises, Utility Installations, and Alterations in good order, condition and repair (whether or not the portion of the Premises requiring repairs, or the means of repairing the same, are reasonably or readily accessible to Lessee, and whether or not the need for such repairs occurs as a result of Lessee's use, any prior use, the elements or the age of such portion of the Premises), including, but not limited to, all equipment or facilities, such as plumbing, heating, ventilating, air-conditioning, electrical, lighting facilities, boilers, pressure vessels, fire protection system, fixtures, walls (interior and exterior), foundations, ceilings, roofs, floors, windows, doors, plate glass, skylights, landscaping, driveways, parking lots, fences, retaining walls, signs, sidewalks and parkways located in, on, or adjacent to the Premises. Lessee, in keeping the Premises in good order, condition and repair, shall exercise and perform good,



maintenance practices, specifically including the procurement and maintenance of the service contracts required by Paragraph 7.1 (b) below. Lessee's obligations shall include restorations, replacements or renewals when necessary to keep the Premises and all improvements thereon or a part thereof in good order, condition and state of repair. Lessee shall, during the term of this Lease, keep the exterior appearance of the Building in a first-class condition consistent with the exterior appearance of other similar facilities of comparable age and size in the vicinity, including, when necessary, the exterior repainting of the Building. Lessor shall non-exclusively assign to Lessee all warranties obtained by Lessor related to the Base Building.

(b) SERVICE CONTRACTS. Lessee shall, at Lessee's sole expense, procure and maintain contracts, with copies to Lessor, in customary form and substance for, and with contractors specializing and experienced in the maintenance of the following equipment and improvements, if any, if and when installed on the Premises (the "BASIC ELEMENTS"): (i) HVAC equipment, (ii) boiler, and pressure vessels, (iii) fire extinguishing systems, including fire alarm and/or smoke detection, (iv) landscaping and irrigation systems, (v) roof covering and drains, (vi) driveways and parking lots, (vii) clarifiers (viii) basic utility feed to the perimeter of the Building, and (ix) any other equipment, if reasonably required by Lessor.

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(c) REPLACEMENT. Subject to Lessee's indemnification of Lessor as set forth in Paragraph 8.7 below, and without relieving Lessee of liability resulting from Lessee's failure to exercise and perform good maintenance practices, if the Basic Elements described in Paragraph 7.1 (b) cannot be repaired other than at a cost which is in excess of 50% of the cost of replacing such Basic Elements, then such Basic Elements shall be replaced by Lessor, and the cost thereof shall be prorated between the Parties and Lessee shall only be obligated to pay, each month during the remainder of the term of this Lease, on the date on which Base Rent is due, an amount equal to the product of multiplying the cost of such replacement by a fraction, the numerator of which is one, and the denominator of which is the number of months of the useful life of such replacement as such useful life is specified pursuant to Federal income tax regulations or guidelines for depreciation thereof (including interest on the unamortized balance as is then commercially reasonable in the judgment of Lessor's accountants), with Lessee reserving the right to prepay its obligation at any time.

#### 7.2. LESSOR'S OBLIGATIONS.

Subject to the provisions of Paragraphs 2.2 (Condition), 2.3 (Compliance), 9 (Damage or Destruction) and 14 (Condemnation), it is intended by the Parties hereto that Lessor have no obligation, in any manner whatsoever, to repair and maintain the Premises, or the equipment therein, all of which obligations are intended to be that of the Lessee. It is the intention of the Parties that the terms of this Lease govern the respective obligations of the Parties as to maintenance and repair of the Premises, and they expressly waive the benefit of any statute now or hereafter in effect to the extent it is inconsistent with the terms of this Lease.

#### 7.3. UTILITY INSTALLATIONS; TRADE FIXTURES; ALTERATIONS.

(a) DEFINITIONS; CONSENT REQUIRED. The term "UTILITY INSTALLATIONS" refers to all floor and window coverings, air lines, power panels, electrical distribution, security and fire protection systems, communication systems, lighting fixtures, HVAC equipment, plumbing, and fencing in or on the Premises. The term "TRADE FIXTURES" shall mean Lessee's machinery and equipment that can be removed without doing

material damage to the Premises. The term "ALTERATIONS" shall mean any modification of the improvements, other than Utility Installations or Trade Fixtures, whether by addition or deletion. "LESSEE OWNED ALTERATIONS AND/OR UTILITY INSTALLATIONS" are defined as Alterations and/or Utility Installations made by Lessee that are not yet owned by Lessor pursuant to Paragraph 7.4(a). Lessee shall not make any Alterations or Utility Installations to the Premises without Lessor's prior written consent. Lessee may, however, make non-structural Utility Installations to the interior of the Premises (excluding the roof) without such consent but upon notice to Lessor, as long as they are not visible from the outside, do not involve puncturing, relocating or removing the roof or any existing walls, and the cumulative cost thereof during this Lease as extended does not exceed \$50,000 in the aggregate or \$10,000 in any one year.

(b) CONSENT. Any Alterations or Utility Installations that Lessee shall desire to make and which require the consent of the Lessor shall be presented to Lessor in written form with detailed plans. Consent shall be deemed conditioned upon Lessee's: (i) acquiring all applicable governmental permits, (ii) furnishing Lessor with copies of both the permits and the plans and specifications prior to commencement of the work, and (iii) compliance with all conditions of

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said permits and other Applicable Requirements in a prompt and expeditious manner. Any Alterations or Utility Installations shall be performed in a workmanlike manner with good and sufficient materials. Lessee shall promptly upon completion furnish Lessor with as-built plans and specifications. For work which costs an amount equal to the greater of one month's Base Rent, or \$10,000, Lessor may condition its consent upon Lessee providing a lien and completion bond in an amount equal to one and one-half times the estimated cost of such Alteration or Utility Installation and/or upon Lessee's posting an additional Security Deposit with Lessor.

(c) INDEMNIFICATION. Lessee shall pay, when due, all claims for labor or materials furnished or alleged to have been furnished to or for Lessee at or for use on the Premises, which claims are or may be secured by any mechanic's or materialmen's lien against the Premises or any interest therein. Lessee shall give Lessor not less than ten (10) days' notice prior to the commencement of any work in, on or about the Premises, and Lessor shall have the right to post notices of non-responsibility. If Lessee shall contest the validity of any such lien, claim or demand, then Lessee shall, at its sole expense defend and protect itself, Lessor and the Premises against the same and shall pay and satisfy any such adverse judgment that may be rendered thereon before the enforcement thereof. If Lessor shall require, Lessee shall furnish a surety bond in an amount equal to one and one-half times the amount of such contested lien, claim or demand, indemnifying Lessor against liability for the same. If Lessor elects to participate in any such action, Lessee shall pay Lessor's attorneys' fees and costs.

#### 7.4. OWNERSHIP; REMOVAL; SURRENDER; AND RESTORATION.

(a) OWNERSHIP. Subject to Lessor's right to require removal or elect ownership as hereinafter provided, all Alterations and Utility Installations made by Lessee shall be the property of Lessee, but considered a part of the Premises. Lessor may, at any time, elect in writing to be the owner of all or any specified part of the Lessee Owned Alterations and Utility Installations except for those items listed on Exhibit B ("Protected Lessee Owned Alterations"). Unless otherwise instructed per Paragraph 7.4(b) hereof, all Lessee Owned Alterations and Utility Installations (except for Protected Lessee Owned Alterations) shall, at the expiration or termination of this Lease, unless removed by

Lessee pursuant to this Lease, become the property of Lessor and be surrendered by Lessee with the Premises.

(b) REMOVAL. By delivery to Lessee of written notice from Lessor not earlier than ninety (90) and not later than thirty (30) days prior to the end of the term of this Lease, Lessor may require that any or all Lessee Owned Alterations or Utility Installations be removed by the expiration or termination of this Lease. Lessor may require the removal at any time of all or any part of any Lessee Owned Alterations or Utility Installations made without the required consent.

(c) SURRENDER/RESTORATION. Lessee shall surrender the Premises by the Expiration Date or any earlier termination date, with all of the improvements, parts and surfaces thereof broom clean and free of debris, and in good operating order, condition and state of repair, ordinary wear and tear excepted. "Ordinary wear and tear" shall not include any damage or deterioration that would have been prevented by good maintenance practice. Lessee shall repair any damage occasioned by the installation, maintenance or removal of Trade Fixtures, Lessee Owned Alterations and/or Utility Installations, furnishings, and equipment as well as the removal of any storage tank installed by or for Lessee, and the removal, replacement, or remediation of any soil, material or groundwater contaminated by Lessee. Trade Fixtures shall remain the property of Lessee and shall be removed by Lessee. The failure by Lessee to timely vacate the Premises

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pursuant to this Paragraph 7.4(c) without the express written consent of Lessor shall constitute a holdover under the provisions of Paragraph 26 below.

## 8. INSURANCE; INDEMNITY.

### 8.1. PAYMENT FOR INSURANCE.

Lessee shall pay for all insurance required under Paragraph 8 except to the extent of the cost attributable to liability insurance carried by Lessor under Paragraph 8.2(b) in excess of \$2,000,000 per occurrence. Premiums for policy periods commencing prior to or extending beyond the Lease term shall be prorated to correspond to the Lease term. Payment shall be made by Lessee to Lessor within ten (10) days following receipt of an invoice.

### 8.2. LIABILITY INSURANCE.

(a) CARRIED BY LESSEE. Lessee shall obtain and keep in force a Commercial General Liability Policy of insurance protecting Lessee and Lessor against claims for bodily injury, personal injury and property damage based upon or arising out of the ownership, use, occupancy or maintenance of the Premises and all areas appurtenant thereto. Such insurance shall be on an occurrence basis providing single limit coverage in an amount not less than \$2,000,000 per occurrence with an "ADDITIONAL INSURED-MANAGERS OR LESSORS OF PREMISES ENDORSEMENT" and contain the "AMENDMENT OF THE POLLUTION EXCLUSION ENDORSEMENT" for damage caused by heat, smoke or fumes from a hostile fire. The Policy shall not contain any intra-insured exclusions as between insured persons or organizations, but shall include coverage for liability assumed under this Lease as an "insured contract" for the performance of Lessee's indemnity obligations under this Lease. The limits of said insurance shall not, however, limit the liability of Lessee nor relieve Lessee of any obligation hereunder. All insurance carried by Lessee shall be primary to and not contributory with any similar insurance carried by Lessor, whose insurance shall be considered excess insurance

only.

(b) CARRIED BY LESSOR. Lessor shall maintain liability insurance as described in Paragraph 8.2(a), in addition to, and not in lieu of, the insurance required to be maintained by Lessee. Lessee shall not be named as an additional insured therein.

### 8.3. PROPERTY INSURANCE - BUILDING, IMPROVEMENTS AND RENTAL VALUE.

(a) BUILDING AND IMPROVEMENTS. The Insuring Party shall obtain and keep in force a policy or policies in the name of Lessor, with loss payable to Lessor, any groundlessor, and to any Lender(s) insuring loss or damage to the Premises. The amount of such insurance shall be equal to the full replacement cost of the Premises, as the same shall exist from time to time, or the amount required by any Lenders, but in no event more than the commercially reasonable and available insurable value thereof. If Lessor is the Insuring Party, however, Lessee Owned Alterations and Utility Installations, Trade Fixtures, and Lessee's personal property shall be insured by Lessee under Paragraph 8.4 rather than by Lessor. If the coverage is available and commercially appropriate, such policy or policies shall insure against all risks of direct physical loss or damage (except the perils of flood and/or earthquake unless required by a Lender), including coverage for debris removal and the enforcement of any Applicable Requirements requiring the upgrading, demolition, reconstruction or replacement of any portion of the Premises

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as the result of a covered loss. Said policy or policies shall also contain an agreed valuation provision in lieu of any coinsurance clause, waiver of subrogation, and inflation guard protection causing an increase in the annual property insurance coverage amount by a factor of not less than the adjusted U.S. Department of Labor Consumer Price Index for All Urban Consumers for the city nearest to where the Premises are located. If such insurance coverage has a deductible clause, the deductible amount shall not exceed \$10,000 per occurrence, and Lessee shall be liable for such deductible amount in the event of an insured Loss.

(b) RENTAL VALUE. The Insuring Party shall obtain and keep in force a policy or policies in the name of Lessor with loss payable to Lessor and any Lender, insuring the loss of the full Rent for one (1) year. Said insurance shall provide that in the event the Lease is terminated by reason of an insured loss, the period of indemnity for such coverage shall be extended beyond the date of the completion of repairs or replacement of the Premises, to provide for one full year's loss of Rent from the date of any such loss. Said insurance shall contain an agreed valuation provision in lieu of any coinsurance clause, and the amount of coverage shall be adjusted annually to reflect the projected Rent otherwise payable by Lessee, for the next twelve (12) month period. Lessee shall be liable for any deductible amount in the event of such loss.

(c) ADJACENT PREMISES. If the Premises are part of a larger building, or of a group of buildings owned by Lessor which are adjacent to the Premises, the Lessee shall pay for any increase in the premiums for the property insurance of such building or buildings if said increase is caused by Lessee's acts, omissions, use or occupancy of the Premises.

### 8.4. LESSEE'S PROPERTY/BUSINESS INTERRUPTION INSURANCE.

(a) PROPERTY DAMAGE. Lessee shall obtain and maintain insurance

coverage on all of Lessee's personal property, Trade Fixtures, and Lessee Owned Alterations and Utility Installations. Such insurance shall be full replacement cost coverage with a deductible of not to exceed \$5,000 per occurrence. The proceeds from any such insurance shall be used by Lessee for the replacement of personal property, Trade Fixtures and Lessee Owned Alterations and Utility Installations. Lessee shall provide Lessor with written evidence that such insurance is in force.

(b) BUSINESS INTERRUPTION. Lessee shall obtain and maintain loss of income and extra expense insurance in amounts as will reimburse Lessee for direct or indirect loss of earnings attributable to all perils commonly insured against by prudent lessees in the business of Lessee or attributable to prevention of access to the Premises as a result of such perils.

(c) NO REPRESENTATION OF ADEQUATE COVERAGE. Lessor makes no representation that the limits or forms of coverage of insurance specified herein are adequate to cover Lessee's property, business operations or obligations under this Lease.

#### 8.5. INSURANCE POLICIES.

Insurance required herein shall be by companies duly licensed or admitted to transact business in the state where the Premises are located, and maintaining during the policy term a "General Policyholders Rating" of at least B+, V, as set forth in the most current issue of "Best's Insurance Guide", or such other rating as may be required by a Lender. Lessee shall not do or permit to be done anything which invalidates the required insurance policies. Lessee shall, prior to the Early Possession Date, deliver to Lessor certified copies of policies of such insurance or certificates evidencing the existence and amounts of the required insurance. No

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such policy shall be cancelable or subject to modification except after thirty (30) days prior written notice to Lessor. Lessee shall, at least thirty (30) days prior to the expiration of such policies, furnish Lessor with evidence of renewals or "insurance binders" evidencing renewal thereof, or Lessor may order such insurance and charge the cost thereof to Lessee, which amount shall be payable by Lessee to Lessor upon demand. Such policies shall be for a term of at least one year, or the length of the remaining term of this Lease, whichever is less. If either Party shall fail to procure and maintain the insurance required to be carried by it, the other Party may, but shall not be required to, procure and maintain the same.

#### 8.6. WAIVER OF SUBROGATION.

Without affecting any other rights or remedies, Lessee and Lessor each hereby release and relieve the other, and waive their entire right to recover damages against the other, for loss of or damage to its property arising out of or incident to the perils required to be insured against herein. The effect of such releases and waivers is not limited by the amount of insurance carried or required, or by any deductibles applicable hereto. The Parties agree to have their respective property damage insurance carriers waive any right to subrogation that such companies may have against Lessor or Lessee, as the case may be, so long as the insurance is not invalidated thereby.

#### 8.7. INDEMNITY.

Except for Lessor's gross negligence or willful misconduct, Lessee shall indemnify, protect, defend and hold harmless the Premises, Lessor and its agents, Lessor's master or ground lessor, partners and Lenders, from

and against any and all claims, loss of rents and/or damages, liens, judgments, penalties, attorneys' and consultants' fees, expenses and/or liabilities arising out of, involving, or in connection with, the use and/or occupancy of the Premises by Lessee. If any action or proceeding is brought against Lessor by reason of any of the foregoing matters, Lessee shall upon notice defend the same at Lessee's expense by counsel reasonably satisfactory to Lessor and Lessor shall cooperate with Lessee in such defense. Lessor need not have first paid any such claim in order to be defended or indemnified.

#### 8.8. EXEMPTION OF LESSOR FROM LIABILITY.

Subject to the provisions of Section 6 of the Work Letter, Lessor shall not be liable for injury or damage to the person or goods, wares, merchandise or other property of Lessee, Lessee's employees, contractors, invitees, customers, or any other person in or about the Premises, whether such damage or injury is caused by or results from fire, steam, electricity, gas, water or rain, or from the breakage, leakage, obstruction or other defects of pipes, fire sprinklers, wires, appliances, plumbing, HVAC or lighting fixtures, or from any other cause, whether the said injury or damage results from conditions arising upon the Premises or upon other portions of the Building of which the Premises are a part, or from other sources or places. Lessor shall not be liable for any damages arising from any act or neglect of any other tenant of Lessor. Notwithstanding Lessor's negligence or breach of this Lease, Lessor shall under no

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circumstances be liable for injury to Lessee's business or for any loss of income or profit therefrom.

#### 9. DAMAGE OR DESTRUCTION.

##### 9.1. DEFINITIONS.

(a) "PREMISES PARTIAL DAMAGE" shall mean damage or destruction to the improvements on the Premises, other than Lessee Owned Alterations and Utility Installations, which can reasonably be repaired in six (6) months or less from the date of the damage or destruction. Lessor shall notify Lessee in writing within thirty (30) days from the date of the damage or destruction as to whether or not the damage is Partial or Total.

(b) "PREMISES TOTAL DESTRUCTION" See Addendum Paragraph 53

(c) "INSURED LOSS" shall mean damage or destruction to improvements on the Premises' other than Lessee Owned Alterations and Utility Installations and Trade Fixtures, which was caused by an event required to be covered by the insurance described in Paragraph 8.3(a), irrespective of any deductible amounts or coverage limits involved.

(d) "REPLACEMENT COST" shall mean the cost to repair or rebuild the improvements owned by Lessor at the time of the occurrence to their condition existing immediately prior thereto, including demolition, debris removal and upgrading required by the operation of Applicable Requirements, and without deduction for depreciation.

(e) "HAZARDOUS SUBSTANCE CONDITION" shall mean the occurrence or discovery of a condition involving the presence of, or a contamination by, a Hazardous Substance as defined in Paragraph 6.2(a), in, on, or under the Premises.

##### 9.2. PARTIAL DAMAGE - INSURED LOSS.

If a Premises Partial Damage that is an Insured Loss occurs, then Lessor shall, at Lessor's expense, repair such damage (but not Lessee's Trade Fixtures or Lessee Owned Alterations and Utility Installations) as soon as reasonably possible and this Lease shall continue in full force and effect; provided, however, that Lessee shall, at Lessor's election, make the repair of any damage or destruction the total cost to repair of which is \$10,000 or less, and, in such event, Lessor shall make any applicable insurance proceeds available to Lessee on a reasonable basis for that purpose. Notwithstanding the foregoing, if the required insurance was not in force or the insurance proceeds are not sufficient to effect such repair, the Insuring Party shall promptly contribute the shortage in proceeds (except as to the deductible which is Lessee's responsibility) as and when required to complete said repairs. In the event, however, such shortage was due to the fact that, by reason of the unique nature of the improvements, full replacement cost insurance coverage was not commercially reasonable and available, Lessor shall have no obligation to pay for the shortage in insurance proceeds or to fully restore the unique aspects of the Premises unless Lessee provides Lessor with the funds to cover same, or adequate assurance thereof, within ten (10) days following receipt of written notice of such shortage and request therefor. If Lessor receives said funds or adequate assurance thereof within said ten (10) day period, the party responsible for making the repairs shall complete them as soon as reasonably possible and this Lease shall remain in full force and effect. If such funds or assurance are not received, Lessor may nevertheless elect by

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written notice to Lessee within ten (10) days thereafter to: (i) make such restoration and repair as is commercially reasonable with Lessor paying any shortage in proceeds, in which case this Lease shall remain in full force and effect, or (ii) have this Lease terminate thirty (30) days thereafter. Lessee shall not be entitled to reimbursement of any funds contributed by Lessee to repair any such damage or destruction. Premises Partial Damage due to flood or earthquake shall be subject to Paragraph 9.3, notwithstanding that there may be some insurance coverage, but the net proceeds of any such insurance shall be made available for the repairs if made by either Party.

#### 9.3. PARTIAL DAMAGE - UNINSURED LOSS.

If a Premises Partial Damage that is not an Insured Loss occurs, unless caused by a negligent or willful act of Lessee (in which event Lessee shall make the repairs at Lessee's expense), Lessor may either: (i) repair such damage as soon as reasonably possible at Lessor's expense, in which event this Lease shall continue in full force and effect, or (ii) terminate this Lease by giving written notice to Lessee within thirty (30) days after receipt by Lessor of knowledge of the occurrence of such damage. Such termination shall be effective sixty (60) days following the date of such notice. In the event Lessor elects to terminate this Lease, Lessee shall have the right within ten (10) days after receipt of the termination notice to give written notice to Lessor of Lessee's commitment to pay for the repair of such damage without reimbursement from Lessor. Lessee shall provide Lessor with said funds or satisfactory assurance thereof within thirty (30) days after making such commitment. In such event this Lease shall continue in full force and effect, and Lessor shall proceed to make such repairs as soon as reasonably possible after the required funds are available. If Lessee does not make the required commitment, this Lease shall terminate as of the date specified in the termination notice. (See Addendum Paragraph 54)

#### 9.4. TOTAL DESTRUCTION.

Notwithstanding any other provision hereof, if a Premises Total Destruction occurs, this Lease shall terminate sixty (60) days following such Destruction. If the damage or destruction was caused by the gross negligence or willful misconduct of Lessee, Lessor shall have the right to recover Lessor's damages from Lessee, except as provided in Paragraph 8.6.

9.5. DAMAGE NEAR END OF TERM.

If at any time during the last six (6) months of this Lease there is damage for which the cost to repair exceeds one (1) month's Base Rent, whether or not an Insured Loss, Lessor may terminate this Lease effective sixty (60) days following the date of occurrence of such damage by giving a written termination notice to Lessee within thirty (30) days after the date of occurrence of such damage. Notwithstanding the foregoing, if Lessee at that time has an exercisable option to extend this Lease or to purchase the Premises, then Lessee may preserve this Lease by, (a) exercising such option and (b) subject to Lessor's obligation under Paragraph 9.3 as revised, providing Lessor with any shortage in insurance proceeds (or adequate assurance thereof) needed to make there pairs on or before the earlier of (i) the date which is ten days after Lessee's receipt of Lessor written notice purporting to terminate this Lease, or (ii) the day prior to the date upon which such option expires. If Lessee duly exercises such option during such period and provides

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Lessor with funds (or adequate assurance thereof to cover any shortage in insurance proceeds), Lessor shall, at Lessor's commercially reasonable expense, repair such damage as soon as reasonably possible and this Lease shall continue in full force and effect. If Lessee fails to exercise such option and provide such funds or assurance during such period, then this Lease shall terminate on the date specified in the termination notice and Lessee's option shall be extinguished. (See Addendum Paragraph 55)

9.6. ABATEMENT OF RENT; LESSEE'S REMEDIES.

(a) ABATEMENT. In the event of Premises Partial Damage or Premises Total Destruction or a Hazardous Substance Condition for which Lessee is not responsible under this Lease, the Rent payable by Lessee for the period required for the repair, remediation or restoration of such damage shall be abated in proportion to the degree to which Lessee's use of the Premises is impaired, but not to exceed the proceeds received from the Rental Value insurance. All other obligations of Lessee hereunder shall be performed by Lessee, and Lessor shall have no liability for any such damage, destruction, remediation, repair or restoration except as provided herein.

(b) REMEDIES. If Lessor shall be obligated to repair or restore the Premises and does not commence, in a substantial and meaningful way, such repair or restoration within ninety (90) days after such obligation shall accrue, Lessee may, at any time prior to the commencement of such repair or restoration, give written notice to Lessor and to any Lenders of which Lessee has actual notice, of Lessee's election to terminate this Lease on a date not less than sixty (60) days following the giving of such notice. If Lessee gives such notice and such repair or restoration is not commenced within thirty (30) days thereafter, this Lease shall terminate as of the date specified in said notice. If the repair or restoration is commenced within said thirty (30) days, this Lease shall continue in full force and effect. "COMMENCE" shall mean either the unconditional authorization of the preparation of the required plans, or the beginning of the actual work on the Premises, whichever first occurs.



9.7. TERMINATION - ADVANCE PAYMENTS.

Upon termination of this Lease pursuant to Paragraph 6.2(g) or Paragraph 9, an equitable adjustment shall be made concerning advance Base Rent and any other advance payments made by Lessee to Lessor. Lessor shall, in addition, return to Lessee so much of Lessee's Security Deposit as has not been, or is not then required to be, used by Lessor.

9.8. WAIVE STATUTES.

Lessor and Lessee agree that the terms of this Lease shall govern the effect of any damage to or destruction of the Premises with respect to the termination of this Lease and hereby waive the provisions of any present or future statute to the extent inconsistent herewith.

10. REAL PROPERTY TAXES.

10.1. DEFINITION OF "REAL PROPERTY TAXES."

As used herein, the term "REAL PROPERTY TAXES" shall include any form of assessment; real estate, general, special, ordinary or extraordinary or ad valorem real estate taxes and assessments (other than inheritance, personal income or estate taxes); and/or improvement bond imposed upon or levied against any legal or equitable interest of Lessor in the Premises,

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by any authority having the direct or indirect power to tax and where the funds are generated with reference to the Building address and where the proceeds so generated are to be applied by the city, county or other local taxing authority of a jurisdiction within which the Premises are located. The term "REAL PROPERTY TAXES" shall also include any tax, fee, levy, assessment or charge, or any increase therein, imposed by reason of events occurring during the term of this Lease, including but not limited to, a change in the ownership of the Premises.

10.2.

(a) PAYMENT OF TAXES. Lessee shall pay the Real Property Taxes applicable to the Premises during the term of this Lease. Subject to Paragraph 10.2(b), all such payments shall be made at least ten (10) days prior to any delinquency date. Lessee shall promptly furnish Lessor with satisfactory evidence that such taxes have been paid. If any such taxes shall cover any period of time prior to or after the expiration or termination of this Lease, Lessee's share of such taxes shall be prorated to cover only that portion of the tax bill applicable to the period that this Lease is in effect, and Lessor shall reimburse Lessee for any overpayment. If Lessee shall fail to pay any required Real Property Taxes, Lessor shall have the right to pay the same, and Lessee shall reimburse Lessor therefor upon demand.

(b) ADVANCE PAYMENT. In the event Lessee incurs a late charge on any Rent payment, Lessor may, at Lessor's option, estimate the current Real Property Taxes, and require that such taxes be paid in advance to Lessor by Lessee, either: (i) in a lump sum amount equal to the installment due, at least twenty (20) days prior to the applicable delinquency date, or (ii) monthly in advance with the payment of the Base Rent. If Lessor elects to require payment monthly in advance, the monthly payment shall be an amount equal to the amount of the estimated installment of taxes divided by the number of months remaining before the month in which said installment becomes delinquent. When the actual amount of the applicable tax bill is known, the amount of such equal monthly advance payments shall be adjusted as required to provide the

funds needed to pay the applicable taxes. If the amount collected by Lessor is insufficient to pay such Real Property Taxes when due, Lessee shall pay Lessor, upon demand, such additional sums as are necessary to pay such obligations. All monies paid to Lessor under this Paragraph may be intermingled with other monies of Lessor and shall not bear interest. In the event of a Breach by Lessee in the performance of its obligations under this Lease, then any balance of funds paid to Lessor under the provisions of this Paragraph may, at the option of Lessor, be treated as an additional Security Deposit.

#### 10.3. JOINT ASSESSMENT.

If the Premises are not separately assessed, Lessee's liability shall be an equitable proportion of the Real Property Taxes for all of the land and improvements included within the tax parcel assessed, such proportion to be conclusively determined by Lessor from the respective valuations assigned in the assessor's work sheets or such other information as may be reasonably available.

#### 10.4. PERSONAL PROPERTY TAXES.

Lessee shall pay, prior to delinquency, all taxes assessed against and levied upon Lessee Owned Alterations, Utility Installations, Trade Fixtures, furnishings, equipment and all personal property

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of Lessee. When possible, Lessee shall cause such property to be assessed and billed separately from the real property of Lessor. If any of Lessee's said personal property shall be assessed with Lessor's real property, Lessee shall pay Lessor the taxes attributable to Lessee's property within ten (10) days after receipt of a written statement.

#### 11. UTILITIES.

Lessee shall pay for all water, gas, heat, light, power, telephone, trash disposal and other utilities and services supplied to the Premises, together with any taxes thereon. If any such services are not separately metered to Lessee, Lessee shall pay a reasonable proportion, to be determined by Lessor, of all charges jointly metered.

#### 12. ASSIGNMENT AND SUBLETTING.

##### 12.1. LESSOR'S CONSENT REQUIRED.

(a) Lessee shall not voluntarily or by operation of law assign, transfer, mortgage or encumber (collectively, "ASSIGN OR ASSIGNMENT") or sublet all or any part of Lessee's interest in this Lease or in the Premises without Lessor's prior written consent which consent shall be deemed granted unless Lessor has refused its consent by notice to Lessee given within twenty (20) days following notice from Lessee requesting such consent and which consent shall not be unreasonably withheld or delayed.

(b) See Addendum Paragraph 56

(c) The involvement of Lessee or its assets in any transaction, or series of transactions (by way of merger, sale, acquisition, financing, transfer, leveraged buy-out or otherwise), whether or not a formal assignment or hypothecation of this Lease or Lessee's assets occurs, which results or will result in a reduction of the Net Worth of Lessee by an amount greater than twenty-five percent (25%) of such Net Worth as it was represented at the time of the execution of this Lease or at the time of the most recent assignment to which Lessor has consented, or as it exists immediately prior to said transaction or

transactions constituting such reduction, whichever was or is greater, shall be considered an assignment of this Lease to which Lessor may withhold its consent. "NET WORTH OF LESSEE" shall mean the net worth of Lessee (excluding any guarantors) established under generally accepted accounting principles.

(d) An assignment or subletting without consent shall, at Lessor's option, be a Default curable after notice per Paragraph 13.1 (c), or a noncurable Breach without the necessity of any notice and grace period. If Lessor elects to treat such unapproved assignment or subletting as a noncurable Breach, Lessor may either: (i) terminate this Lease, or (ii) upon thirty (30) days written notice, increase the monthly Base Rent to one hundred ten percent (110%) of the Base Rent then in effect. Further, in the event of such Breach and rental adjustment, (i) the purchase price of any option to purchase the Premises held by Lessee shall be subject to similar adjustment to one hundred ten percent (110%) of the price previously in effect, and (ii) all fixed and non-fixed rental adjustments scheduled during the remainder of the Lease term shall be increased to One Hundred Ten Percent (110%) of the scheduled adjusted rent.

#### 12.2. TERMS AND CONDITIONS APPLICABLE TO ASSIGNMENT AND SUBLETTING.

(a) Regardless of Lessors consent, any assignment or subletting shall not: (i) be effective without the express written assumption by such assignee or sublessee of the obligations of

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Lessee under this Lease; (ii) release Lessee of any obligations hereunder; or (iii) alter the primary liability of Lessee for the payment of Rent or for the performance of any other obligations to be performed by Lessee.

(b) Lessor may accept Rent or performance of Lessee's obligations from any person other than Lessee pending approval or disapproval of an assignment. The acceptance of Rent or performance shall not constitute a waiver or estoppel of Lessor's right to exercise its remedies for Lessee's Default or Breach.

(c) Lessor's consent to any assignment or subletting shall not constitute a consent to any subsequent assignment or subletting.

(d) In the event of any Default or Breach by Lessee, Lessor may proceed directly against Lessee, any Guarantors or anyone else responsible for the performance of Lessee's obligations under this Lease, including any assignee or sublessee, without first exhausting Lessor's remedies against any other person or entity responsible therefore to Lessor, or any security held by Lessor.

(e) Each request for consent to an assignment or subletting shall be in writing, accompanied by information relevant to Lessor's determination as to the financial and operational responsibility and appropriateness of the proposed assignee or sublessee, including but not limited to the intended use and/or required modification of the Premises, if any, together with a fee of \$ 1,000, as consideration for Lessor's considering and processing said request. Lessee agrees to provide Lessor with such other or additional information and/or documentation as may be reasonably requested.

(f) Any assignee of, or sublessee under, this Lease shall, by reason of accepting such assignment or entering into such sublease, be deemed to have assumed and agreed to conform and comply with each and every term in, covenant, condition and obligation herein to be observed or performed by Lessee during the term of said assignment or sublease,

other than such obligations as are contrary to or inconsistent with provisions of an assignment or sublease to which Lessor has specifically consented to in writing.

### 12.3. ADDITIONAL TERMS AND CONDITIONS APPLICABLE TO SUBLETTING.

The following terms and conditions shall apply to any subletting by Lessee of all or any part of the Premises and shall be deemed included in all subleases under this Lease whether or not expressly incorporated therein:

(a) Lessee hereby assigns and transfers to Lessor all of Lessee's interest in all Rent payable on any sublease, and Lessor may collect such Rent and apply same toward Lessee's obligations under this Lease; provided, however, that until a Breach shall occur in the performance of Lessee's obligations, Lessee may collect said Rent. Lessor shall not, by reason of the foregoing or any assignment of such sublease, nor by reason of the collection of Rent, be deemed liable to the sublessee for any failure of Lessee to perform and comply with any of Lessee's obligations to such sublessee. Lessee hereby irrevocably authorizes and directs any such sublessee, upon receipt of a written notice from Lessor stating that a Breach exists in the performance of Lessee's obligations under this Lease, to pay to Lessor all Rent due and to become due under the sublease, Sublessee shall rely upon any such notice from Lessor and shall pay all Rents to Lessor without any obligation or right to inquire as to whether such Breach exists, notwithstanding any claim from Lessee to the contrary. Any sublease rent in excess of the Rent and other payments due to Lessor from Lessee hereunder shall belong to Lessee.

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(b) In the event of a Breach by Lessee, Lessor may, at its option, require sublessee to attorn to Lessor, in which event Lessor shall undertake the obligations of the sublessor under such sublease from the time of the exercise of said option to the expiration of such sublease; provided, however, Lessor shall not be liable for any prepaid rents or security deposit paid by such sublessee to such sublessor or for any prior Defaults or Breaches of such sublessor.

(c) Any matter requiring the consent of the sublessor under a sublease shall also require the consent of Lessor.

(d) No sublessee shall further assign or sublet all or any part of the Premises without Lessor's prior written consent.

(e) Lessor shall deliver a copy of any notice of Default or Breach by Lessee to the sublessee, who shall have the right to cure the Default of Lessee within the grace period, if any, specified in such notice. The sublessee shall have a right of reimbursement and offset from and against Lessee for any such Defaults cured by the sublessee.

### 13. DEFAULT; BREACH; REMEDIES.

#### 13.1. DEFAULT; BREACH.

A "DEFAULT" is defined as a failure by the Lessee to comply with or perform any of the terms, covenants, conditions or rules under this Lease. A "BREACH" is defined as the occurrence of one or more of the following Defaults, and the failure of Lessee to cure such Default within any applicable grace period:

(a) The abandonment of the Premises; or the vacating of the Premises without providing a commercially reasonable level of security, or where the coverage of the property insurance described in Paragraph

8.3 is jeopardized as a result thereof, or without providing reasonable assurances to minimize potential vandalism.

(b) The failure of Lessee to make any payment of Rent or any Security Deposit required to be made by Lessee hereunder, whether to Lessor or to a third party, when due, to provide reasonable evidence of insurance or surety bond, or to fulfill any obligation under this Lease which endangers or threatens life or property, where such failure continues for a period of three (3) business days following written notice to Lessee.

(c) The failure by Lessee to provide (i) reasonable written evidence of compliance with Applicable Requirements, (ii) the service contracts, (iii) the rescission of an unauthorized assignment or subletting, (iv) a Tenancy Statement, (v) a requested subordination, (vi) evidence concerning any guaranty and/or Guarantor, (vii) any document requested under Paragraph 42 (easements), or (viii) any other documentation or information which Lessor may reasonably require of Lessee under the terms of this Lease, where any such failure continues for a period of ten (10) days following written notice to Lessee.

(d) A Default by Lessee as to the terms, covenants, conditions or provisions of this Lease, or of the rules adopted under Paragraph 40 hereof, other than those described in subparagraphs 13.1 (a), (b) or (c), above, where such Default continues for a period of thirty (30) days after written notice; provided, however, that if the nature of Lessee's Default is such that more than thirty (30) days are reasonably required for its cure, then it shall not be deemed to be a Breach if Lessee commences such cure within said thirty (30) day period and thereafter diligently prosecutes such cure to completion.

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(e) The occurrence of any of the following events: (i) the making of any general arrangement or assignment for the benefit of creditors; (ii) becoming a "debtor" as defined in 11 U.S.C. Section 101 or any successor statute thereto (unless, in the case of a petition filed against Lessee, the same is dismissed within sixty (60) days); (iii) the appointment of a trustee or receiver to take possession of substantially all of Lessee's assets located at the Premises or of Lessee's interest in this Lease, where possession is not restored to Lessee within thirty (30) days; or (iv) the attachment, execution or other judicial seizure of substantially all of Lessee's assets located at the Premises or of Lessee's interest in this Lease, where such seizure is not discharged within thirty (30) days; provided, however, in the event that any provision of this subparagraph 13.1 (e) is contrary to any applicable law, such provision shall be of no force or effect, and not affect the validity of the remaining provisions.

(f) The discovery that any financial statement of Lessee or of any Guarantor given to Lessor was materially false.

(g) If the performance of Lessee's obligations under this Lease is guaranteed: (i) the death of a Guarantor; (ii) the termination of a Guarantor's liability with respect to this Lease other than in accordance with the terms of such guaranty; (iii) a Guarantor's becoming insolvent or the subject of a bankruptcy filing; (iv) a Guarantor's refusal to honor the guaranty; or (v) a Guarantor's breach of its guaranty obligation on an anticipatory basis, and Lessee's failure, within sixty (60) days following written notice of any such event, to provide written alternative assurance or security, which, when coupled with the then existing resources of Lessee, equals or exceeds the combined financial resources of Lessee and the Guarantors that existed at the time of execution of this Lease.

13.2. REMEDIES.

If Lessee fails to perform any of its affirmative duties or obligations, within ten (10) days after written notice (or in case of any emergency, without notice), Lessor may, at its option, perform such duty or obligation on Lessee's behalf, including but not limited to the obtaining of reasonably required bonds, insurance policies, or governmental licenses, permits or approvals. The costs and expenses of any such performance by Lessor shall be due and payable by Lessee upon receipt of invoice therefor. In the event of a Breach, Lessor may, with or without further notice or demand, and without limiting Lessor in the exercise of any right or remedy which Lessor may have by reason of such Breach:

(a) Terminate Lessee's right to possession of the Premises by any lawful means, in which case this Lease shall terminate and Lessee shall immediately surrender possession to Lessor. In such event Lessor shall be entitled to recover from Lessee: (i) the unpaid Rent which had been earned at the time of termination; (ii) the worth at the time of award of the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that the Lessee proves could have been reasonably avoided; (iii) the worth at the time of award of the amount by which the unpaid rent for the balance of the term after the time of award exceeds the amount of such rental loss that the Lessee proves could be reasonably avoided; and (iv) any other amount necessary to compensate Lessor for all the detriment proximately caused by the Lessee's failure to perform its obligations under this Lease or which in the ordinary course of things would be likely to result therefrom, including but not limited to the cost of recovering possession of the Premises, expenses of relating, including

necessary renovation and alteration of the Premises, reasonable attorneys' fees, and that portion of any leasing commission paid by Lessor in connection with this Lease applicable to the unexpired term of this Lease. The worth at the time of award of the amount referred to in provision (iii) of the immediately preceding sentence shall be computed by discounting such amount at the discount rate of the Federal Reserve Bank of the District within which the Premises are located at the time of award plus one percent (1%). Efforts by Lessor to mitigate damages caused by Lessee's Breach of this Lease shall not waive Lessor's right to recover the balance of damages owing under Paragraph 12. If termination of this Lease is obtained through the provisional remedy of unlawful detainer, Lessor shall have the right to recover in such proceeding any unpaid Rent and damages as are recoverable therein, or Lessor may reserve the right to recover all or any part thereof in a separate suit. If the notice and grace period required under Paragraph 13.1 was not previously given, a notice to pay rent or quit, or to perform or quit given to Lessee under the unlawful detainer statute shall also constitute the notice required by Paragraph 13.1. In such case, the applicable grace period required by Paragraph 13.1 and the unlawful detainer statute shall run concurrently, and the failure of Lessee to cure the Default within the greater of the two such grace periods shall constitute both an unlawful detainer and a Breach of this Lease entitling Lessor to the remedies provided for in this Lease and/or by said statute.

(b) Continue the Lease and Lessee's right to possession and recover the Rent as it becomes due, in which event Lessee may sublet or assign, subject only to reasonable limitations. Acts of maintenance, efforts to relet, and/or the appointment of a receiver to protect the Lessor's interests, shall not constitute a termination of the Lessee's right to possession.

(c) Pursue any other remedy now or hereafter available under the laws or judicial decisions of the state wherein the Premises are located. The expiration or termination of this Lease and/or the termination of Lessee's right to possession shall not relieve Lessee from liability under any indemnity provisions of this Lease as to matters occurring or accruing during the term hereof or by reason of Lessee's occupancy of the Premises.

(d) If the nature of Lessee's obligation is such that more than thirty (30) days are reasonably required for its performance, then Lessee, shall not be in breach if performance is commenced within such thirty (30) day period and thereafter diligently pursued to completion.

#### 13.3. INDUCEMENT RECAPTURE.

Intentionally Omitted

#### 13.4. LATE CHARGES.

Lessee hereby acknowledges that late payment by Lessee of Rent will cause Lessor to incur costs not contemplated by this Lease, the exact amount of which will be extremely difficult to ascertain. Such costs include, but are not limited to, processing and accounting charges, and late charges which may be imposed upon Lessor by any Lender. Accordingly, if any Rent shall not be received by Lessor within five (5) days after such amount shall be due, then, without any requirement for notice to Lessee, Lessee shall pay to Lessor a one-time late charge equal to three percent (3%) of each such overdue amount. The Parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Lessor will incur by

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reason of such late payment. Acceptance of such late charge by Lessor shall in no event constitute a waiver of Lessee's Default or Breach with respect to such overdue amount nor prevent the exercise of any of the other rights and remedies granted hereunder. In the event that a late charge is payable hereunder, whether or not collected, for three (3) consecutive installments of Base Rent, then notwithstanding any provision of this Lease to the contrary, Base Rent shall, at Lessor's option, become due and payable quarterly in advance.

#### 13.5. INTEREST.

Any monetary payment due Lessor hereunder, other than late charges and Rent received by Lessor within five (5) days after such amount shall be due, not received by Lessor, when due as to scheduled payments (such as Base Rent) or within thirty (30) days following the date on which it was due for non-scheduled payment, shall bear interest from the date when due, as to scheduled payments, or the thirty-first (31st) day after it was due as to non-scheduled payments. The interest ("Interest") charged shall be equal to the prime rate reported in the Wall Street Journal as published closest prior to the date when due plus four percent (4%), but shall not exceed the maximum rate allowed by law. Interest is payable in addition to the potential late charge provided for in Paragraph 13.4.

#### 13.6. BREACH BY LESSOR.

(a) NOTICE OF BREACH. Lessor shall not be deemed in breach of this Lease unless Lessor fails within a reasonable time to perform an obligation required to be performed by Lessor. For purposes of this Paragraph, a reasonable time shall in no event be less than thirty (30) days after receipt by Lessor, and any Lender whose name and address shall have been furnished Lessee in writing for such purpose, of written notice specifying wherein such obligation

of Lessor has not been performed; provided, however, that if the nature of Lessor's obligation is such that more than thirty (30) days are reasonably required for its performance, then Lessor shall not be in breach if performance is commenced within such thirty (30) day period and thereafter diligently pursued to completion.

(b) PERFORMANCE BY LESSEE ON BEHALF OF LESSOR. In the event that neither Lessor nor Lender cures said breach within thirty (30) days after receipt of said notice, or if having commenced said cure they do not diligently pursue it to completion, then Lessee may elect to cure said breach at Lessee's expense and offset from Rent an amount equal to the greater of one month's Base Rent or the Security Deposit, and to pay an excess of such expense under protest, reserving Lessee's right to reimbursement from Lessor. Lessee shall document the cost of said cure and supply said documentation to Lessor.

#### 14. CONDEMNATION.

If the Premises or any portion thereof are taken under the power of eminent domain or sold under the threat of the exercise of said power (collectively "CONDEMNATION"), this Lease shall terminate as to the part taken as of the date the condemning authority takes title or possession, whichever first occurs. If more than ten percent (10%) of any building portion of the Premises, or more than twenty-five percent (25%) of the land area portion of the Premises not occupied by any building, is taken by Condemnation, Lessee may, at Lessee's option, to be exercised in writing within ten (10) days after Lessor shall have given Lessee written notice of such taking (or

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in the absence of such notice, within ten (10) days after the condemning authority shall have taken possession) terminate this Lease as of the date the condemning authority takes such possession. If Lessee does not terminate this Lease in accordance with the foregoing, this Lease shall remain in full force and effect as to the portion of the Premises remaining, except that the Base Rent shall be reduced in proportion to the reduction in utility of the Premises caused by such Condemnation. See Addendum Paragraph 57. All Alterations and Utility Installations made to the Premises by Lessee, for purposes of Condemnation only, shall be considered the property of the Lessee and Lessee shall be entitled to any and all compensation which is payable therefor. In the event that this Lease is not terminated by reason of the Condemnation, Lessor shall repair any damage to the Premises caused by such Condemnation.

#### 15. BROKERS' FEE.

15.1.

[Intentionally omitted]

15.2. ASSUMPTION OF OBLIGATIONS.

[Intentionally omitted]

15.3. REPRESENTATIONS AND INDEMNITIES OF BROKER RELATIONSHIPS.

Lessee and Lessor each represent and warrant to the other that it has had no dealings with any person, firm, broker or finder (other than the Brokers, if any) in connection with this Lease, and that no one other than said named Brokers it, entitled to any commission or finder's fee in connection herewith. Lessee and Lessor do each hereby agree to indemnify, protect, defend and hold the other harmless from and against liability for compensation or charges which may be claimed by any such unnamed broker, finder or other similar party by reason of any dealings or actions of the Indemnifying Party, including any costs, expenses, and/or attorneys' fees reasonably incurred with respect thereto.



16. ESTOPPEL CERTIFICATES.

(a) Each Party (as "RESPONDING PARTY") shall within ten (10) days after written notice from the other Party (the "REQUESTING PARTY") execute, acknowledge and deliver to the Requesting Party a statement in writing in form similar to the then most current "ESTOPPEL CERTIFICATE" form published by the American Industrial Real Estate Association, plus such additional information, confirmation and/or statements as may be reasonably requested by the Requesting Party.

(b) If the Responding Party shall fail to execute or deliver the Estoppel Certificate within such ten day period, the Requesting Party may execute an Estoppel Certificate stating that: (i) the Lease is in full force and effect without modification except as may be represented by the Requesting Party, (ii) there are no uncured defaults in the Requesting Party's performance, and (iii) if Lessor is the Requesting Party, not more than one month's Rent has been paid in advance. Prospective purchasers and encumbrancers may rely upon the Requesting Party's Estoppel

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Certificate, and the Responding Party shall be estopped from denying the truth of the facts contained in said Certificate.

(c) If Lessor desires to finance, refinance, or sell the Premises, or any part thereof, Lessee and all Guarantors shall deliver to any potential lender or purchaser designated by Lessor such financial statements as may be reasonably required by such lender or purchaser, including, but not limited to, Lessee's financial statements for the past three (3) years. All such financial statements shall be received by Lessor and such lender or purchaser in confidence and shall be used only for the purposes herein set forth.

17. DEFINITION OF LESSOR.

The term "Lessor" as used herein shall mean the owner or owners at the time in question of the fee title to the Premises, or, if this is a sublease, of the Lessee's interest in the prior lease. In the event of a transfer of Lessor's title or interest in the Premises or this Lease, Lessor shall deliver to the transferee or assignee (in cash or by credit) any unused Security Deposit held by Lessor. Except as provided in Paragraph 15, upon such transfer or assignment and delivery of the Security Deposit, as aforesaid, the prior Lessor shall be relieved of all liability with respect to the obligations and/or covenants under this Lease thereafter to be performed by the Lessor. Subject to the foregoing, the obligations and/or covenants in this Lease to be performed by the Lessor shall be binding only upon the Lessor as hereinabove defined. Notwithstanding the above, and subject to the provisions of Paragraph 20 below, the original Lessor under this Lease, and all subsequent holders of the Lessor's interest in this Lease shall remain liable and responsible with regard to the potential duties and liabilities of Lessor pertaining to Hazardous Substances as outlined in Paragraph 6 above.

18. SEVERABILITY.

The invalidity of any provision of this Lease, as determined by a court of competent jurisdiction, shall in no way affect the validity of any other provision hereof.

19. DAYS.

Unless otherwise specifically indicated to the contrary, the word "days" as used in this Lease shall mean and refer to calendar days.

20. LIMITATION ON LIABILITY.

Subject to the provisions of Paragraph 17 above, the obligations of Lessor under this Lease shall not constitute personal obligations of the individual partners of Lessor or its or their individual, partners, directors, officers or shareholders, and Lessee shall look to the Premises, and to no other assets of Lessor, for the satisfaction of any liability of Lessor with respect to this Lease, and shall not seek recourse against the individual partners of Lessor, or its or their individual partners, directors, officers or shareholders, or any of their personal assets for such satisfaction.

21. TIME OF ESSENCE.

Time is of the essence with respect to the performance of all obligations to be performed or observed by the Parties under this Lease.

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22. NO PRIOR OR OTHER AGREEMENTS; BROKER DISCLAIMER.

This Lease contains all agreements between the Parties with respect to any matter mentioned herein, and no other prior or contemporaneous agreement or understanding shall be effective.

23. NOTICES.

23.1. NOTICE REQUIREMENTS.

All notices required or permitted by this Lease shall be in writing and may be delivered in person (by hand or by courier) or may be sent by regular, certified or registered mail or U.S. Postal Service Express Mail, with postage prepaid, or by facsimile transmission, and shall be deemed sufficiently given if served in a manner specified in this Paragraph 23. The addresses noted adjacent to a Party's signature on this Lease shall be that Party's address for delivery or mailing of notices. Either Party may by written notice to the other specify a different address for notice, except that upon Lessee's taking possession of the Premises, the Premises. Shall constitute Lessee's address for notice. A copy of all notices to Lessor shall be concurrently transmitted to such party or parties at such addresses as Lessor may from time to time hereafter designate in writing.

23.2. DATE OF NOTICE.

Any notice sent by registered or certified mail, return receipt requested, shall be deemed given on the date of delivery shown on the receipt card, or if no delivery date is shown, the postmark thereon. If sent by regular mail the notice shall be deemed given forty-eight (48) hours after the same is addressed as required herein and mailed with postage prepaid. Notices delivered by United States Express Mail or overnight courier that guarantee next day delivery shall be deemed given twenty-four (24) hours after delivery of the same to the Postal Service or courier. Notices transmitted by facsimile transmission or similar means shall be deemed delivered upon telephone confirmation of receipt, provided a copy is also delivered via delivery or mail. If notice is received on a Saturday, Sunday or legal holiday, it shall be deemed received on the next business day.

24. WAIVERS.

No waiver by either Lessor or Lessee of the Default or Breach of any term, covenant or condition hereof by the other, shall be deemed a waiver of any other term, covenant or condition hereof, or of any subsequent Default or Breach by the other of the same or of any other term, covenant or condition hereof. Lessor's or Lessee's consent to, or approval of, any act shall not be deemed to

render unnecessary the obtaining of the other's consent to, or approval of, any subsequent or similar act by the other requiring approval of the other hereunder, or be construed as the basis of an estoppel to enforce the provision or provisions of this Lease requiring such consent. The acceptance of Rent by Lessor shall not be a waiver of any Default or Breach by Lessee. Any payment by Lessee may be accepted by Lessor on account of monies or damages due Lessor, notwithstanding any qualifying statements or conditions made by Lessee in connection therewith, which such statements and/or conditions shall be of no force or effect whatsoever

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unless specifically agreed to in writing by Lessor at or before the time of deposit of such payment.

25. RECORDING.

Either Lessor or Lessee shall, upon request of the other, execute, acknowledge and deliver to the other a short form memorandum of this Lease for recording purposes. The Party requesting recordation shall be responsible for payment of any fees applicable thereto.

26. NO RIGHT TO HOLDOVER.

Lessee has no right to retain possession of the Premises or any part thereof beyond the expiration or termination of this Lease. In the event that Lessee holds over, then the Base Rent shall be increased to one hundred fifty percent (150%) of the Base Rent applicable during the month immediately preceding the expiration or termination. Nothing contained herein shall be construed as consent by Lessor to any holding over by Lessee.

27. CUMULATIVE REMEDIES.

No remedy or election hereunder shall be deemed exclusive but shall, wherever possible, be cumulative with all other remedies at law or in equity.

28. COVENANTS AND CONDITIONS; CONSTRUCTION OF AGREEMENT.

All provisions of this Lease to be observed or performed by Lessee are both covenants and conditions. In construing this Lease, all headings and titles are for the convenience of the Parties only and shall not be considered a part of this Lease. Whenever required by the context, the singular shall include the plural and vice versa. This Lease shall not be construed as if prepared by one of the Parties, but rather according to its fair meaning as a whole, as if both Parties had prepared it.

29. BINDING EFFECT; CHOICE OF LAW.

This Lease shall be binding upon the parties, their successors and assigns and be governed by the laws of the State in which the Premises are located. Any litigation between the Parties hereto concerning this Lease shall be initiated in the county in which the Premises are located.

30. SUBORDINATION; ATTORMENT; NON-DISTURBANCE.

30.1. SUBORDINATION.

This Lease and any Option granted hereby shall be subject and subordinate to any ground lease, mortgage, deed of trust, or other hypothecation or security device (collectively, "Security Device"), now or hereafter placed upon the Premises, to any and all advances made on the security thereof, and to all renewals, modifications, and extensions thereof. Lessee agrees that the holders of any such Security Devices (in this Lease together referred to as "Lessor's Lender") shall have no liability or obligation to perform any of the obligations of Lessor

under this Lease. Any Lender may elect to have this Lease and/or any Option granted hereby superior to the lien of its Security Device by giving written notice thereof to Lessee, whereupon this Lease and such Options shall be deemed prior to such Security Device, notwithstanding the relative dates of the documentation or recordation thereof.

30.2. ATTORNTMENT.

Subject to the non-disturbance provisions of Paragraph 30.3, Lessee agrees to attorn to a Lender or any other party who acquires ownership of the Premises by reason of a foreclosure of a Security Device, and that in the event of such foreclosure, such new owner shall not: (1) be liable for any act or omission of any prior lessor or with respect to events occurring prior to acquisition of ownership; (ii) be subject to any offsets or defenses which Lessee might have against any prior lessor; or (iii) be bound by prepayment of more than one (1) month's rent.

30.3. NON-DISTURBANCE.

With respect to Security Devices entered into by Lessor after the execution of this Lease, Lessee's subordination of this Lease shall be subject to receiving a commercially reasonable non-disturbance agreement (a "NON-DISTURBANCE AGREEMENT") from the Lender which Non-Disturbance Agreement provides that Lessee's possession of the Premises, and this Lease, including any options to extend the term hereof, will not be disturbed so long as Lessee is not in Breach hereof and attorns to the record owner of the Premises. Further, within sixty (60) days after the execution of this Lease, Lessor shall use its commercially reasonable efforts to obtain a Non-Disturbance Agreement from the holder of any pre-existing Security Device which is secured by the Premises. In the event that Lessor is unable to provide the Non-Disturbance Agreement within said sixty (60) days, then Lessee may, at Lessee's option, terminate this Lease so long as notice of such election to terminate is given to Lessor within ten (10) days following the end of such sixty (60) day period.

30.4. SELF-EXECUTING.

The agreements contained in this Paragraph 30 shall be effective without the execution of any further documents; provided, however, that, upon written request from Lessor or a Lender in connection with a sale, financing or refinancing of the Premises, Lessee and Lessor shall execute such further writings as may be reasonably required to separately document any subordination, attornment and/or Non-Disturbance Agreement provided for herein.

31. ATTORNEYS' FEES.

If any Party brings an action or proceeding involving the Premises to enforce the terms hereof or to declare rights hereunder, the Prevailing Party (as hereafter defined) in any such proceeding, action, or appeal thereon, shall be entitled to reasonable attorneys' fees. Such fees may be awarded in the same suit or recovered in a separate suit, whether or not such action or proceeding is pursued to decision or judgment. The term, "Prevailing Party" shall include, without limitation, a Party who substantially obtains or defeats the relief sought, as the case may be, whether by compromise, settlement, judgment, or the abandonment by the other Party of its claim or defense. The attorneys' fees award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all attorneys' fees reasonably incurred. In addition, Lessor shall be entitled to attorneys' fees, costs and expenses incurred in the preparation and service of notices of Default and consultations in connection therewith, whether or not a legal action is subsequently commenced

in connection with such Default or resulting Breach.

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32 LESSOR'S ACCESS; SHOWING PREMISES; REPAIRS.

See Addendum Paragraph 58

33 AUCTIONS.

Lessee shall not conduct, nor permit to be conducted, any auction upon the Premises without Lessor's prior written consent. Lessor shall not be obligated to exercise any standard of reasonableness in determining whether to permit an auction.

34. SIGNS.

Except for ordinary "For Sublease" signs, Lessee shall not place any sign upon the Premises without Lessor's prior written consent. All signs must comply with all Applicable Requirements.

35. TERMINATION; MERGER.

Unless specifically stated otherwise in writing by Lessor and except as provided in a non-disturbance agreement between Lessor and any subtenant, the voluntary or other surrender of this Lease by Lessee, the mutual termination or cancellation hereof, or a termination hereof by Lessor for Breach by Lessee, shall automatically terminate any sublease or lesser estate in the Premises; provided, however, that Lessor may elect to continue any one or all existing subtenancies. Lessor's failure within ten (10) days following any such event to elect to the contrary by written notice to the holder of any such lesser interest, shall constitute Lessor's election to have such event constitute the termination of such interest.

36. CONSENTS.

Except as otherwise provided herein, wherever in this Lease the consent of a Party is required to an act by or for the other Party, such consent shall not be unreasonably withheld or delayed. Lessor's actual reasonable costs and expenses (including, but not limited to, architects', attorneys', engineers' and other consultants' fees) incurred in the consideration of, or response to, a request by Lessee for any Lessor consent, including, but not limited to, consents to an assignment, a subletting or the presence or use of a Hazardous Substance, shall be paid by Lessee upon receipt of an invoice and supporting documentation therefor. Lessor's consent to any act, assignment or subletting shall not constitute an acknowledgment that no Default or Breach by Lessee of this Lease exists, nor shall such consent be deemed a waiver of any then existing Default or Breach, except as may be otherwise specifically stated in writing by Lessor at the time of such consent. The failure to specify herein any particular condition to Lessor's consent shall not preclude the imposition by Lessor at the time of consent of such further or other conditions as are then reasonable with reference to the particular matter for which consent is being given. In the event that either Party disagrees with any determination made by the other hereunder and reasonably requests the reasons for such determination, the determining party shall furnish its reasons in writing and in reasonable detail within ten (10) business days following such request.

37. GUARANTOR.

37.1. EXECUTION.

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The Guarantors, if any, shall each execute a guaranty in the form most recently published by the American Industrial Real Estate Association, and each such Guarantor shall have the same obligations as Lessee under this Lease.

#### 37.2. DEFAULT.

It shall constitute a Default of the Lessee if any Guarantor fails or refuses, upon request to provide: (a) evidence of the execution of the guaranty, including the authority of the party signing on Guarantor's behalf to obligate Guarantor, and in the case of a corporate Guarantor, a certified copy of a resolution of its board of directors authorizing the making of such guaranty, (b) current financial statements, (c) a Tenancy Statement, or (d) written confirmation that the guaranty is still in effect.

#### 38. QUIET POSSESSION.

Subject to payment by Lessee of the Rent and performance of all of the covenants, conditions and provisions on Lessee's part to be observed and performed under this Lease, Lessee shall have quiet possession and quiet enjoyment of the Premises during the term hereof.

#### 39. OPTIONS.

##### 39.1. DEFINITION.

"OPTION" shall mean: (a) the right to extend the term of or renew this Lease or to extend or renew any lease that Lessee has on other property of Lessor; (b) the right of first refusal or first offer to lease either the Premises or other property of Lessor; (c) the right to purchase or the right of first refusal to purchase the Premises or other property of Lessor.

##### 39.2. INTENTIONALLY OMITTED.

##### 39.3. MULTIPLE OPTIONS.

In the event that Lessee has any multiple Options to extend or renew this Lease, a later Option cannot be exercised unless the prior Options have been validly exercised.

##### 39.4. EFFECT OF DEFAULT ON OPTIONS.

(a) Lessee shall have no right to exercise an Option: (i) during the period commencing with the giving of any notice of Default and continuing until said Default is cured, (ii) during the period of time any Rent is unpaid (without regard to whether notice thereof is given Lessee), (iii) during the time Lessee is in Breach of this Lease which Breach has not been cured, or (iv) in the event that Lessee has been given three (3) or more notices of separate Default, whether or not the Defaults are cured, during the six (6) month period immediately preceding the exercise of the Option.

(b) The period of time within which an Option may be exercised shall not be extended or enlarged by reason of Lessee's inability to exercise an Option because of the provisions of Paragraph 39.4(a).

(c) An Option shall terminate and be of no further force or effect, notwithstanding Lessee's due and timely exercise of the Option, if, after such exercise and prior to the commencement of the extended term, (1) Lessee fails to pay Rent for a period of thirty (30) days

after such Rent becomes due (without any necessity of Lessor to give notice thereof), (ii) Lessor gives to Lessee three (3) or more notices of separate Default, whether or not the Defaults are cured, or (iii) if Lessee commits a Breach of this Lease which Breach has not been cured.

40. MULTIPLE BUILDINGS.

If the Premises are a part of a group of buildings controlled by Lessor, Lessee agrees that it will observe all reasonable rules and regulations which Lessor may make from time to time for the management, safety, and care of said properties, including the care and cleanliness of the grounds and including the parking, loading and unloading of vehicles, and that Lessee will pay its fair share of common expenses incurred in connection therewith.

41. SECURITY MEASURES.

Lessee hereby acknowledges that the rental payable to Lessor hereunder does not include the cost of guard service or other security measures, and that Lessor shall have no obligation whatsoever to provide same. Lessee assumes all responsibility for the protection of the Premises, Lessee, its agents and invitees and their property from the acts of third parties.

42. RESERVATIONS.

Lessor reserves to itself the right, from time to time, to grant, without the consent or joinder of Lessee, such easements, rights and dedications that Lessor deems necessary, and to cause the recordation of parcel maps and restrictions, so long as such easements, rights, dedications, maps and restrictions do not unreasonably interfere with the use of the Premises by Lessee, or the interconnection of the Premises with adjacent premises, as contemplated by Addendum Paragraph 60. Lessee agrees to sign any documents reasonably requested by Lessor to effectuate any such easement rights, dedication, map or restrictions.

43. PERFORMANCE UNDER PROTEST

If at any time a dispute shall arise as to any amount or sum, of money to be paid by one Party to the other under the provisions hereof, the Party against whom the obligation to pay the money is asserted shall have the right to make payment "under protest" and such payment shall not be regarded as a voluntary payment and there shall survive the right on the part of said Party to institute suit for recovery of such sum. If it shall be adjudged that there was no legal obligation on the part of said Party to pay such sum or any part thereof, said Party shall be entitled to recover such sum or so much thereof as it was not legally required to pay.

44. AUTHORITY.

If either Party hereto is a corporation, trust, limited liability company, partnership, or similar entity, each individual executing this Lease on behalf of such entity represents and warrants that he or she is duly authorized to execute and deliver this Lease on its behalf. Each Party shall, within thirty (30) days after request, deliver to the other Party satisfactory evidence of such authority.

45. CONFLICT.

Any conflict between the printed provisions of this Lease and the typewritten or handwritten provisions shall be controlled by the typewritten or handwritten provisions.

46. OFFER.

Preparation of this Lease by either Party or their agent and submission of same to the other Party shall not be deemed an offer to lease to the other Party. This Lease is not intended to be binding until executed and delivered by all Parties hereto.

47. AMENDMENTS.

This Lease may be modified only in writing, signed by the Parties in interest at the time of the modification. As long as they do not materially change Lessee's obligations hereunder, Lessee agrees to make such reasonable non-monetary modifications to this, Lease as may be reasonably required by a Lender in connection with the obtaining of normal financing or refinancing of the Premises.

48. MULTIPLE PARTIES.

If more than one person or entity is named herein as either Lessor or Lessee, such multiple Parties shall have joint and several responsibility to comply with the terms of this Lease.

49. MEDIATION AND ARBITRATION OF DISPUTES.

An Addendum requiring the Mediation of all disputes between the Parties and/or Brokers arising out of this Lease x is is not attached to this Lease.

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LESSOR AND LESSEE HAVE CAREFULLY READ AND REVIEWED THIS LEASE AND EACH TERM AND PROVISION CONTAINED HEREIN, AND BY THE EXECUTION OF THIS LEASE SHOW THEIR INFORMED AND VOLUNTARY CONSENT THERETO. THE PARTIES HEREBY AGREE THAT, AT THE TIME THIS LEASE IS EXECUTED, THE TERMS OF THIS LEASE ARE COMMERCIALY REASONABLE AND EFFECTUATE THE INTENT AND PURPOSE OF LESSOR AND LESSEE WITH RESPECT TO THE PREMISES.

[SIGNATURES APPEAR ON THE FOLLOWING PAGE]

[THIS IS THE SIGNATURE PAGE FOR THAT CERTAIN LEASE DATED OCTOBER 15, 1999 BY AND BETWEEN CHAMPAGNE BUILDING GROUP, LP AS LESSOR AND SKECHERS USA, INC. AS LESSEE WITH RESPECT TO PROPERTY LOCATED AT 1670 S. CHAMPAGNE AVENUE, ONTARIO]

The parties hereto have executed this Lease at the place and on (the dates specified above their respective signatures.

Executed at: Manhattan Beach, Calif.

Executed at: Manhattan Beach, CA

On: 11/16/99

On: November 15, 1999

By LESSOR:

By LESSEE:

Champagne Building Group, LP, a California limited partnership  
D and D Champagne, LLC, California limited liability company, General Partner

Skechers USA, Inc., a Delaware corporation

By: DONALD W. GILMOUR

By: DAVID WEINBERG

Name Printed: DONALD W. GILMOUR

Name Printed: David Weinberg

Title: Managing Member

Title: Chief Financial Officer

By: [SIGNATURE ILLEGIBLE]

By: Philip Paccione

Name Printed: [ILLEGIBLE]

Name Printed: Philip Paccione

Address: 2240 University Drive, Suite 100

Address: 228 Manhattan Beach Blvd.



Telephone: 949-722-7058

Telephone: 310-318-2082

Facsimile: 949-722-8565

Facsimile: 310-798-7961

LEGAL DESCRIPTION

THE LAND REFERRED TO HEREIN IS SITUATED IN THE STATE OF CALIFORNIA, COUNTY OF SAN BERNARDINO, AND IS DESCRIBED AS FOLLOWS:

PARCELS 18 AND 23 OF PARCEL MAP NO. 9252, AS SHOWN BY MAP ON FILE IN BOOK 107 PAGE(S) 75 THROUGH 82, INCLUSIVE, OF PARCEL MAPS, RECORDS OF SAN BERNARDINO COUNTY, CALIFORNIA;

ALSO EXCEPTING THEREFROM ALL MINERAL AND ALL MINERAL RIGHTS, OIL AND GAS AND RIGHTS THERETO TOGETHER WITH SOLE, EXCLUSIVE AND PERPETUAL RIGHT TO EXPLORE FOR, REMOVE AND DISPOSE OF, SAID MINERALS BY ANY MEANS OR METHODS SUITABLE, BUT WITHOUT ENTERING UPON OR USING THE SURFACE OF SAID LANDS AND IN SUCH A MANNER AS NOT TO DAMAGE SURFACE OF SAID LANDS OR TO INTERFERE WITH THE USE THEREOF, AS CONVEYED TO UNION PACIFIC LAND RESOURCES CORPORATION BY DEED RECORDED NOVEMBER 23, 1982 AS INSTRUMENT NO. 82-234011 OF OFFICIAL RECORDS.

EXHIBIT A  
WORK LETTER

EXHIBIT A

WORK LETTER

1670 CHAMPAGNE AVENUE, ONTARIO, CA

SKECHERS USA, INC as Tenant and CHAMPAGNE BUILDING GROUP LP as Landlord are executing, simultaneously with this Work Letter, a Standard Industrial/Commercial Single-Tenant Lease-Net (the "Lease"), covering certain Premises at 1670 S. Champagne Avenue, Ontario, California as more particularly described in the Lease. This Work Letter is hereby incorporated into such Lease as an Exhibit thereto. In consideration of the mutual covenants contained in the Lease, Tenant and Landlord hereby agree that the Premises shall be improved in accordance with the provisions of this Work Letter. To the extent that this Work Letter conflicts with any provision in the Lease, the provision of this Work Letter shall govern.

1.1 BASE BUILDING AND RENT.

Landlord and Tenant understand and acknowledge that Landlord has agreed to construct and deliver the "Base Building" to Tenant in exchange for Tenant's agreement to pay the Rent and comply with the other terms and conditions of the Lease.

1.1.1 BASE BUILDING BY LANDLORD.

The "Base Building" shall be constructed by Landlord's contractor at Landlord's sole cost and expense, except for Tenant's responsibilities for portions of the Base Building as set forth in Section 1.1.1.2, in accordance with the "Building Plans and Specifications" identified on the List of Building Plans and Specifications attached as Schedule 2 to this Work Letter, and as closely as reasonably possible substantially in accordance with the Preliminary Construction Schedule attached as Schedule 3 to this Work Letter. The "Base Building" is defined as and is described with particularity in the Building Plans and Specifications and includes, among other things, the items described in Section 1.1.1.1. If there is any conflict between the items described as included in Section 1.1.1.1 and the items of work included in the Building Plans and Specifications, the Building Plans and Specifications shall govern. The Base Building shall be constructed in a good and workmanlike manner and shall comply with all applicable laws, ordinances and codes, and the rules and regulations of all governmental authorities having jurisdiction and shall comply with all applicable insurance regulations.

1.1.1.1 INCLUDED IN BASE BUILDING.

The "Base Building" shall include, among other things, the following elements of the Building:

1.1.1.1. DESIGN, ARCH, ENGINEERING AND CITY PROCESSING.

For building modification to raise the clear height from 30' clear to 39'6" clear;

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1.1.1.2. OFFICE.

Office space at the north side of the warehouse of approximately 2,800 square feet to include three private offices approximately 12 feet x 15 feet. Restrooms to include: one men's with 3 stalls, 3 sinks, 3 urinals, one women's with 5 stalls, 3 sinks. Lunchroom of approximately 1,125 square feet and shall be accessible to the warehouse. Lunchroom and restrooms are per Architect specifications;

1.1.1.3. LIGHTING.

Metal halide warehouse lighting for 20-foot candles (assuming 7 fixtures per aisle for 38 aisles at racking area and on fixture at 30 foot x 32 foot on center in the balance of the building to achieve the 20 foot candles). Racking and aisle alignment information obtained from W.E.I., Skechers' consultant;

1.1.1.4. TRUCK LOADING.

Forty dock high (8'6" x 10") door with dock seal and light package. W.E.I. spec for 40 doors. Blue giant edge of dock levelers Model MD72255M with seal and light package.

1.1.1.1.1 Electrical for lighting and fans

between every other door. 20 4-plex 20 amp plugs.

1.1.1.1.2 12'x14' ground level doors at the north and south end of the building.

1.1.1.1.3 Ramp in back of the building at the rail door. Enlarge door. (12x14).

1.1.1.1.4 Provide two (2) dock high doors on the back of the north side (on the curve) of the building.

1.1.1.1.5 Provide two (2) paved pathways in back of the facility to allow forklift access between the new and existing facilities.

1.1.1.5. CLEAR HEIGHT

39'6" (except for the 1st 6' in front of the loading area by truck doors). This area will be 38';

1.1.1.6. FOIL INSULATED CEILING.

Upgrade the foil to multi-layer over the mezz area room grid 13 to 19. Approximately 60,000 square feet at 30 cents per foot;

1.1.1.7. SKYLIGHT.

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Two and one-half percent (2 1/2%);

1.1.1.8. FANS.

Code-1/2 air change per hour. One additional air changes in total building. Two air changes in north 60,000 square feet in mezz area;

1.1.1.9. SPRINKLERS.

ESFR Specification using K-25 high capacity head increasing pipe size and flow rate so not to need pump;

1.1.1.10 FLOOR.

Floor spec 6" thick with 4000 P.S.I. tensile strength;

1.1.1.11 POWER.

2000 amp, 480/227 Volts, 3 Phase Sub panel to battery charging forklifts, 20 stations;

1.1.1.12 OUTSIDE LIGHTING.

Per Building Plans and specifications.

1.1.1.2 TENANT BASE BUILDING RESPONSIBILITIES.

Tenant has agreed to accept the responsibility to separately pay for the following items of Base Building

work ("Tenant Base Building Responsibilities") even though such items are included within the Building Plans and Specifications:

1.1.1.2.1 ROOF TRUSSES.

Roof trusses have been modified and reengineered to carry additional loads to support Tenant's conveyor system per W.E.L spec and Tenant shall separately pay for the increased costs due to such modifications, which costs are agreed to be \$17,300;

1.1.1.2.2 PAYMENT BY TENANT.

Upon execution of the Lease, Tenant shall pay to Landlord in cash an amount equal to the estimated cost of the item described in Section 1.1.1.2.1 as such amount is set forth in such Section.

1.1.1.3 TENANT REVIEW OF BUILDING PLANS AND SPECIFICATIONS.

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Tenant has reviewed and approved the plans and specifications for the Base Building including, without limitation, the Base Building design, Base Building systems, parking structure, and floor plans referred to on Schedule 2 (collectively, the "Building Plans"). Landlord may make changes to Building Plans without Tenant's consent provided that such changes do not change the size or the exterior dimensions of the Premises, do not cause changes to the Tenant Improvements, do not delay Tenant's construction of the Tenant Improvements, and provided further that the Base Building, when constructed in accordance with such revised Building Plans and Specifications, shall be comparable to, or better than, the Base Building described in the Building Plans and Specifications approved by Tenant.

1.2. TENANT IMPROVEMENTS.

The provisions of this Work Letter pertaining to the construction of Tenant Improvements shall apply only to the extent that Tenant elects to construct improvements within the Premises. Such provisions shall not be interpreted to "require" Tenant to build any Tenant Improvements. The provisions of this Work Letter relating to Tenant Improvements shall apply to the installation by Tenant of Tenant's contemplated "material handling system".

1.2.1. TENANT'S GENERAL CONTRACTOR.

Tenant, through Tenant's general contractor (who shall first be approved by Landlord, which approval shall not be unreasonably withheld or delayed), shall construct within the Premises those improvements (the "Tenant Improvements") shown on the Tenant's Final Space Plans (including, without limitation, the Tenant Base Building Responsibilities), as approved by the Landlord and Tenant pursuant to Section 2 below. Landlord hereby approves WEI as Tenant's general contractor. All Tenant Improvements shall be constructed pursuant to this Work Letter and shall be performed only by Tenant's general contractor pursuant to a construction

contract approved by Landlord as set forth in Section 4.1.1. Tenant shall be responsible for the coordination and supervision of the construction of the Tenant Improvements by Tenant's general contractor. Tenant agrees that Tenant's general contractor shall be licensed and fully insured in the construction of the Tenant Improvements.

1.2.2. TENANT FACILITIES.

Tenant shall have the opportunity to incorporate special Tenant facilities ("Tenant Facilities") into the Premises as part of the Tenant Improvements including, without limitation, a material handling system, facilities for computers, telephone equipment rooms, file rooms, and other special facilities incidental to Tenants operations; provided, however, as follows:

1.2.2.1. COMPLIANCE WITH LAWS.

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All such Tenant Facilities shall comply with all applicable laws, ordinances and codes, and the rules and regulations of all governmental authorities having jurisdiction;

1.2.2.2. FLOOR LOAD WEIGHTS.

The projected load weights per square foot for such areas shall be within the limits set forth in the Building Plans (unless such floors are capable of being reinforced, and Tenant, at Tenant's sole expense, reinforces the floors as, necessary);

1.2.2.3. COMPLIANCE WITH INSURANCE.

All such Tenant Facilities shall comply with all applicable insurance regulations;

1.2.2.4. LANDLORD APPROVAL OF SPECIFICATIONS.

The specifications for such Tenant Facilities have been reasonably approved by Landlord as consistent with the design and engineering specifications for the Base Building;

1.2.2.5. REQUIRED CHANGES TO BASE BUILDING WORK.

To the extent such Tenant Facilities require changes to the Base Building, such changes shall be made by Landlord, at Tenant's cost (all such work shall be charged to Tenant at competitive rates which would be charged by qualified third party contractors of similar quality and reputation as Landlord's contractor if such work were bid out);

1.2.2.6. DELAYS CAUSED BY TENANT FACILITIES.

To the extent the inclusion of such Tenant Facilities or the construction of the Tenant Improvements causes delays of the Substantial Completion of the Base Building by Landlord, the date on which the Landlord shall be deemed to have delivered the Base Building for all purposes with respect to this Work Letter and the Lease shall be the date upon which Landlord would have delivered the Base Building but for the delays

attributable to Tenant Facilities requested by Tenant hereunder.

## 2. PLANS AND SPECIFICATIONS FOR TENANT IMPROVEMENTS

### 2.1. TENANT CONSULTANTS.

Tenant shall retain an architect of its choice and, at Tenant's election, a space planner, each subject to Landlord's approval (which shall not be unreasonably withheld or delayed) to prepare the plans and specifications described hereinafter for the Tenant Improvements.

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### 2.2. TENANT SCHEMATIC SPACE PLANS.

Tenant shall cause its architect (or space planner) to furnish to Landlord for Landlord's approval (which shall not be unreasonably withheld) space plans sufficient to convey the architectural design of the Premises, including without limitation, the location of doors, partitions, electrical and telephone outlets, plumbing fixtures, heavy floor loads and other special requirements, together with reflective ceiling plans, and plans for any improvements to be constructed outside of the Base Building ("Tenant's Schematic Space Plans"). Landlord's approval or disapproval shall be given within ten (10) days of receipt of such plans. If Landlord shall reasonably disapprove of any portion of Tenant's Schematic Space Plans, Landlord shall advise Tenant of Landlord's required revisions, and the reasons therefor. Tenant shall then submit to Landlord, for Landlord's approval, a redesign of Tenant's Schematic Space Plans, incorporating the revisions required by Landlord, as modified by Tenant, which modifications must be approved by Landlord prior to Tenant's submission of the "Tenant's Final Space Plans" (as such term is defined below).

### 2.3. TENANT'S FINAL SPACE PLANS.

Tenant shall cause its architect (or space planner) to prepare from Tenant's approved Tenant's Schematic Space Plans complete architectural plans, drawings and specifications and, utilizing Landlord's mechanical, electrical, life safety and structural engineers, complete engineered mechanical, electrical, life safety, sprinkler, plumbing and structural working drawings for (a) all of the Premises, showing the subdivision, and layout desired by Tenant therefor, and (b) any internal or external communications or special utility facilities which will require conduiting, or other improvements within the Base Building, all in such form and in such detail as may be reasonably required by Landlord (collectively, "Tenant's Final Space Plans"). Tenant's Final Space Plans shall (i) be compatible with the Base Building and with the design and construction of and the equipment and systems within the Base Building including, without limitation, the heating, ventilating and air conditioning, life safety, sprinkler, plumbing and electrical systems; (ii) comply with all applicable laws, ordinances and codes, and the rules and regulations of all governmental authorities having jurisdiction; and (iii) comply with all applicable insurance regulations. Tenant shall submit the Tenant's Final Space Plans for the approval (which shall not be unreasonably withheld or delayed) of Landlord and otherwise in the same manner as provided in Section 2.2 above for approval by Landlord of Tenant's Schematic Space Plans.

### 2.4. QUALITY OF TENANT IMPROVEMENTS.

The Tenant Improvements shall not require extraordinary building services (unless Tenant agrees to pay the excess actual costs associated therewith) or overload the floors. Any required floor reinforcements above the floor load levels set forth in Building Plans shall be at

Tenant's cost.

## 2.5. RESPONSIBILITY FOR GOVERNMENTAL APPROVALS.

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### 2.5.1. TENANT IMPROVEMENTS.

Tenant (or its architect or space planner) shall be responsible, at Tenant's sole cost, for obtaining approval of the Tenant's Final Space Plans by all governmental agencies having jurisdiction of the Premises, together with all other governmental approvals with respect to the installation of the Tenant Improvements, including any necessary building permits and all other necessary permits and the temporary and permanent Certificates of Occupancy for the Premises.

### 2.5.2. BASE BUILDING WORK.

Landlord or Landlord's engineers, at Landlord's cost, shall obtain all necessary approvals, permits and licenses specifically required for the Base Building, including without limitation, electrical, mechanical and structural engineering of the Base Building. Landlord shall reasonably cooperate with Tenant in obtaining all other necessary approvals and permits.

## 2.6. INSPECTION BY LANDLORD.

From time to time during Tenant's construction of the Tenant Improvements, Landlord may inspect the work in place upon the Premises for compliance with the Tenant's Final Space Plans.

## 3. ALLOWANCE FOR WORK AND WORK COST.

### 3.1. TENANT IMPROVEMENT ALLOWANCE.

Tenant shall receive NO allowance from Landlord for the construction of the Tenant Improvements. All Tenant Improvement work shall be contracted by Tenant and the entire Work Cost for any Tenant Improvements shall be paid directly by Tenant.

### 3.2. CHANGES TO BASE BUILDING WORK.

If the Tenant's Final Space Plans or any amendment thereof or supplement thereto shall require changes in the Base Building including any change to accommodate Tenant's Tenant Facilities or the Tenant Improvements pursuant to Section 1.2.2 above, and such proposed changes are acceptable to Landlord, in its reasonable discretion, the cost of such changes shall be paid directly by Tenant. The cost of such changes to the Base Building shall include all direct architectural and/or engineering fees and expenses in connection therewith, including plan check and inspection fees. Landlord shall notify Tenant within ten (10) days following Landlord's receipt of Tenant's Final Space Plans whether or not and, if so, to the estimated extent, shall require changes in the Base Building.

### 3.3. PAYMENT OF TENANT IMPROVEMENT WORK COSTS.

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Tenant shall be responsible for and shall pay directly all costs of the Tenant Improvements and Landlord shall have no responsibility therefor.

### 3.4. CHANGES TO PLANS.

In the event that changes to the Tenant's Schematic Space Plans or Tenant's Final Space Plans are requested by Tenant or required by any governmental agency subsequent to Landlord's approval thereof, except for non-material changes, such changes and the costs thereof shall be forwarded to Landlord for approval (which approval shall not be unreasonably withheld) prior to incorporation into the work, provided, however, that Landlord shall be obligated to approve any changes required by any governmental agency. After Landlord's approval of the changes and the costs thereof, the changes shall be incorporated into the work by means of a change order.

## 4. CONSTRUCTION.

### 4.1. CONSTRUCTION OF TENANT IMPROVEMENTS.

Upon written notice from Landlord that the Base Building has been sufficiently completed and/or the Premises are reasonably available for the construction of the Tenant Improvements hereunder and the Tenant make now take Early Possession (as defined in Paragraph 3.2 of the Lease), Tenant shall have the right, but not the obligation, to take Early Possession and to direct Tenant's contractor to immediately commence and diligently complete construction of the Tenant Improvements.

#### 4.1.1. LANDLORD APPROVAL OF CONSTRUCTION CONTRACT.

Such construction shall be carried out pursuant to a construction contract approved in writing by Landlord, which approval shall not be unreasonably withheld or delayed. Such construction contract shall provide for retention of ten percent (10%) of the monthly progress payments. Landlord shall have the right, but not the obligation, to demand that Tenant promptly cause its contractor(s) to correct any or the following or, if so ordered by Landlord, to stop the work upon the occurrence of any of the following:

##### 4.1.1.1. LIENS.

In the event any materialmen's, mechanic's or other lien is filed against the Premises and not promptly removed, or in the event all subcontractors are not compensated in due course for work performed with respect to the construction of the Tenant Improvements;

##### 4.1.1.2. POOR WORKMANSHIP.

If any portion of the Tenant Improvements constructed under Tenant's direction is of inadequate or inferior quality or workmanship and Tenant does not diligently proceed to replace or repair such inadequate or inferior work upon written notice from Landlord;

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##### 4.1.1.3. TENANT VIOLATION.

If the contractor fails in any material way to adhere to the provisions of the Lease, including, without limitation, the provisions of this Work Letter, and such violation has not been remedied within five (5) business days of Tenant's receipt of written notice from Landlord, or if such violation is of a nature such that it can not be reasonably cured within a five (5)



business days period, if Tenant or its contractor has not commenced to cure within such period and diligently proceeded to cure thereafter;

#### 4.2. TENANT IMPROVEMENT SCHEDULE.

Prior to commencement of any Tenant Improvement work in the Premises, Tenant shall furnish for approval to Landlord in writing a schedule setting forth projected completion dates and showing the deadlines for any actions required to be taken by Landlord and Tenant during such construction.

#### 4.3. LANDLORD APPROVAL OF TENANT SUBCONTRACTORS.

Landlord shall have the right to approve all subcontractors designated by Tenant or Tenant's agents or contractor for work on the Premises with respect to construction of the Tenant Improvements which subcontractors work is material to the construction of the Tenant Improvements or material in relation to the Base Building, which approval shall not be unreasonably withheld or delayed, and which approval or disapproval shall be given by Landlord within ten (10) days after Tenant submits a list of subcontractors for Landlord's approval. Landlord hereby approves WEI as a subcontractor for Tenant.

#### 4.4. REQUIREMENTS FOR CARRYING OUT LANDLORD'S AND TENANT'S WORK.

Landlord and Tenant agree that all construction work shall be carried out at such times as Landlord directs, in accordance with reasonable rules and regulations, promulgated by Landlord and in such a manner as to minimize as much as reasonably possible interference with the work of either Landlord or Tenant, and, without limiting the generality of the foregoing, in accordance with the following:

##### 4.4.1. QUALITY WORK.

Such work shall be performed in a good and workmanlike manner and in accordance with all applicable laws.

##### 4.4.2. BONDS, LICENSE AND INSURANCE.

Prior to Tenant commencing work on the Premises, Tenant shall cause Tenant's contractor to furnish to Landlord, at Tenant or Tenant's contractor's cost, and Landlord shall cause Landlord's contractor to furnish to Tenant, at Landlord or Landlord's contractor's cost, (i) evidence satisfactory to the other that such party's contractor has a valid and appropriate license; and (ii) sufficient evidence that such

contractor is carrying workmen's compensation insurance in statutorily required amounts, together with general liability insurance naming Landlord or Tenant, as the case may be, its lender and its managing agent as additional insureds in such limits and with such insurers as are reasonably appropriate under the circumstances.

##### 4.4.3. LANDLORD RIGHT TO INSPECT.

Landlord shall have the right to enter the Premises at all times to inspect the work and to post notices of nonresponsibility.

##### 4.4.4. NO LIENS.

Tenant shall ensure lien free completion of the Tenant Improvement Work and Landlord shall ensure lien free completion of the Base Building. If a lien is filed and is attributable to the work of the other, the party responsible shall within thirty (30) days of receiving written notice thereof either discharge such lien or, if such party determines to contest such lien, post a bond in accordance with Section 3143 of the California Civil Code releasing the Building and Premises from such lien. If such party fails to discharge such lien or to post such bond to discharge such lien, the other party shall have the right to discharge such lien and to bill the other party for the cost thereof, which cost shall be reimbursed to the party posting such bond within five (5) business days.

#### 4.4.5 CONCURRENT WORK.

It is Landlord's intention to permit Tenant to take Early Possession of the Premises on or before March 1, 2000. When Landlord permits Tenant to take Early Possession, it is likely that Landlord's work on the Base Building will not be complete. Landlord and Tenant agree that if Tenant takes Early Possession before Substantial Completion of the Base Building has occurred that both Landlord and Tenant will cooperate with the other and instruct their respective contractors and subcontractors to cooperate with those of the other and to minimize the interference with the work of the other.

#### 4.4.6 UNION LABOR.

Each of Landlord and Tenant has indicated to the other that they intend to use only non-union labor for work on the Premises. Each party agrees that prior to Landlord or Tenant or their respective contractors or subcontractors permitting union trades to perform work on the Premises, the party so permitting union trades will first notify the other party and shall obtain and deliver to the other party a certificate of non-interference so that injunctive relief would be available should the union trades attempt to interfere with the activities of the non-union trades.

If either Landlord or Tenant or their respective contractors or subcontractors invite or acquiesce in union trades performing work on the Premises and if union

interference should arise during the course of construction as a result of such union trades performing work on the Premises, the party responsible for such union trades performing work on the Premises shall be responsible for promptly resolving such interference and as to such responsible party, such interference shall NOT constitute a Force Majeure event. On the other hand, such interference SHALL constitute a Force Majeure event as to the party not so responsible for such interference.

In the event of union interference that is not the responsibility of either Landlord or Tenant as described in the preceding paragraph, then the party targeted by such union interference shall be responsible for resolving such interference as expeditiously as possible. To the extent any such interference occurs, such interference shall constitute a Force Majeure event for both Landlord and Tenant.

## 5. TENANT ACCESS.

5.1. LANDLORD TO PROVIDE ACCESS.

Landlord shall upon and after the Early Possession Date, during the hours set for in Schedule 1 to this Work Letter ("Access Hours"), provide Tenant and Tenant's employees, space planners, architects, contractors and subcontractors, reasonable access to the Premises, along with adequate electricity and lighting available to the Premises for the purpose of constructing the Tenant Improvements and installing Tenant's furniture, fixtures, equipment (including telephone, communications and computer equipment) and personal property for use in the Premises.

5.2. STOCKING OF MATERIALS.

All stocking of major materials for use in the Tenant Improvements shall be performed after regular business hours.

5.3. SUBJECT TO LANDLORD'S RULES & REGULATIONS.

Subject to Section 5.1 above, Tenant's rights of access, construction and installation hereunder shall be subject to the reasonable rules and the direction of Landlord.

5.4. FREE OF LANDLORD MATERIALS.

Tenant's Lease space shall be free of any debris, and any material or inventory stored by Landlord, prior to Tenant's move-in to the Premises.

6. INDEMNIFICATION.

Tenant hereby indemnifies Landlord and agrees to protect, defend and hold Landlord, its constituent members, affiliates, partners, and their respective agents, officers and employees, harmless from and against any and all losses, costs, liabilities, damages,

demands, claims, causes of action and expenses (including attorneys' fees and court costs) by reason of damage to the Base Building, Premises or the property of others and/or personal injury, including death, which may arise from the Tenant Improvement work in the Premises, whether caused by Tenant, Tenant's contractor or any subcontractor, or anyone directly or indirectly employed by any of them.

Landlord hereby indemnifies Tenant and agrees to protect, defend and hold Tenant, its constituent members, affiliates, partners, and their respective agents, officers and employees, harmless from and against any and all losses, costs, liabilities, damages, demands, claims, causes of action and expenses (including attorneys' fees and court costs) by reason of damage to the Base Building, Premises or the property of others and/or personal injury, including death, which may arise during the construction of the Base Building, whether caused by Landlord, Landlord's contractor or any subcontractor, or anyone directly or indirectly employed by any of them.

7. MISCELLANEOUS.

7.1. TENANT'S ENTRY INTO THE PREMISES PRIOR TO SUBSTANTIAL COMPLETION.

Contractor shall allow Tenant and/or Tenant's agents access to the Premises as of the Early Possession Date prior to the Substantial Completion of the Base Building for the purpose of Tenant and/or Tenant's agents constructing the Tenant Improvements and installing equipment or fixtures (including Tenant's data and telephone equipment

and related cabling) in the Premises.

7.2. TENANT'S REPRESENTATIVE.

Tenant has designated Paul Galliher as its sole representative with respect to the matters set forth in this Tenant Work Letter, who, until further notice to Landlord, shall have full authority and responsibility to act on behalf of the Tenant as required in this Tenant Work Letter.

7.3. LANDLORD'S REPRESENTATIVE.

Landlord has designated Donald Gilmour as its sole representative with respect to the matters set forth in this Tenant Work Letter, who, until further notice to Tenant, shall have full authority and responsibility to act on behalf of the Landlord as required in this Tenant Work Letter.

7.4. PUNCH LIST ITEMS.

Within thirty (30) days of the Substantial Completion of the Premises, Tenant shall provide Landlord a punch list (latent and hidden defects excepted), which punch list shall consist of those decorative and minor mechanical type adjustments which do not materially interfere with Tenant's use of the Premises. Upon receipt of the punch list,

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Landlord shall, at Landlord's sole cost and expense, proceed to diligently remedy all such items within forty-five (45) days of such receipt.

7.5. MISCELLANEOUS CHARGES.

During the period of construction of the Tenant Improvements and Tenant's move into the Premises, neither Tenant nor Tenant's agents shall not be charged for, directly or indirectly, parking, restrooms, HVAC usage, electricity, water, elevator usage, loading dock usage, freight elevator usage, or security.

7.6. STAGING AREA STORAGE SPACE.

During the period commencing on the date of this Lease and prior to the Commencement Date, Tenant shall have the right, without the obligation to pay rent, to use such portion of the Premises designated by Landlord for the purposes of storing and staging Tenant's property. With respect to this free storage space, Tenant shall provide all insurance and any necessary fencing or other protective facilities. Tenant shall hold Landlord harmless and indemnify Landlord from and against any and all loss, liability or cost arising out of or in connection with use of this storage space by Tenant, except to the extent caused by the negligence or willful misconduct of Landlord.

7.7. SECOND STORY OFFICE.

Landlord acknowledges that Tenant may elect to add a second story to the "office" portion of the Premises. The first floor of such "office" is included as part of the Base Building. If Tenant elects to add the second story at any time, such work will be treated as a Tenant Improvement and shall be processed and constructed in accordance with the terms and conditions therefor set forth in this Work Letter. Landlord hereby consents to Tenant's adding such second floor so long as Tenant otherwise complies with this Work Letter as to the construction of such second story addition. Landlord agrees that if Tenant adds such second floor, such second floor will become part of the Premises, and Tenant will not be required to remove it at the expiration of Lease.

INITIALS OF LANDLORD

INITIALS OF TENANT

/s/ [Signature Illegible]

/s/ [Signature Illegible]

SCHEDULE 1 TO WORK LETTER  
CONTRACTOR RULES AND REGULATIONS  
1670 S. CHAMPAGNE AVENUE, ONTARIO, CA

The following are the Rules and Regulations for construction personnel performing work as contractors or suppliers of Tenant at 1670 S. Champagne Avenue, Ontario, California.

1.1 BUILDING ACCESS

1.1.1 PARKING

All personnel shall park on the portion of the Premises designated for such purpose by Landlord from time to time.

1.1.2 STOCKING OF MATERIALS-LARGE QUANTITIES

Stocking of large amounts of materials to be done between 7:00 p.m. and 7:00 a.m.

1.1.1. STOCKING OF MATERIALS-SMALL QUANTITIES

Stocking of small amounts of materials may be done between 7:00 a.m. and 7:00 p.m.

1.1.2. NO STAGING ON SIDEWALKS OR STREET

No materials may be staged (for ANY length of time) on sidewalks or the street.

1.2 JOBSITE

1.2.1 TRASH

Food and debris shall be disposed of in trash receptacles. Each subcontractor shall remove DAILY its construction debris and trash.

1.2.2 FOOD AND DRINK

No food and drink is allowed in areas where finishes have been installed; i.e., carpet, paint, wall coverings, etc.

1.2.3 WORK NEAR DEMISING WALLS

When performing work near the demising wall of an adjacent occupied suite, noisy tasks (screw guns, etc.) must be performed before 7:30 a.m.

1.2.4 NO DRAGGING ACROSS FLOORS

Ladders, other equipment and materials must not be dragged across floors.

#### 1.2.5 USE OF RESTROOMS

Restrooms will not be used to fill buckets, make pastes, wash buckets, etc.

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#### 1.3 SECURITY/PASS DOWNS

Normal working hours are from 7:00 a.m. to 5 p.m.

All work which occurs after normal working hours (between 5 p.m. and 7 a.m.) must be coordinated with the Building Manager.

#### 1.4 FIRE, LIFE SAFETY

Landlord will be notified of all work that affects the various Fire Life Safety systems in the Building. The electrical subcontractors, sprinkler subcontractors, and perhaps other subs must contact Landlord's representative or Landlord's general contractor (via Tenant's general contractor) to arrange for the Building Engineer to disable smoke detectors, bring the Building off-line, drain the sprinkler system, etc., and coordinate inspections with the Ontario Fire Department.

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SCHEDULE 2 TO WORK LETTER  
LIST OF BUILDING PLANS AND SPECIFICATIONS  
1670 S. CHAMPAGNE AVENUE, ONTARIO, CA

#### SOILS REPORT:

Geotechnical Engineering Investigation, Project Number 8104-99 dated May 12, 1999 by NorCal Engineering.

#### CIVILS:

Sheets 1 of 5 through 5 of 5, Grading, Sewer and Water Plans red stamped BID SET SEP 22 1999 by Walden & Associates.

#### ARCHITECTURAL:

Project Manual dated September 27, 1999 and Sheets A0.1, A0.2, A0.2-1 through A0.2-3, A1.1, A2.1, A2.1-R1, A2.1-R2, A2.2, A2.3, A3.1 through A3.6, A4.1 through A4.5, A5.1 and AD.1 through AD.6 red stamped BID SET SEP 22 1999 by Hill Pinckert Architects.

#### STRUCTURAL:

Sheets S-1 through S-4, PNL1 through PNL4, SD1 through SD9, SS1 and SW-1 through SW-3 red stamped BID SET SEP 22 1999 by Mark Dale Associates.

#### ELECTRICAL:

Sheets E1A, E2A and SL1 red stamped BID SET SEP 22 1999 by Gregg Electric.

#### PLUMBING:

Sheet P-1 red stamped BID SET SEP 22 1999 by C W Plumbing & Design, Inc.

MECHANICAL:

Sheet M1 red stamped BID SET SEP 22 1999 by Air Control Systems Inc.

LANDSCAPE:

Sheets T-1 and L-1 through L-9 red stamped BID SET SEP 22 1999 by Hunter Landscape Services.

FIRE SPRINKLER:

Sheets 1 of 9 through 9 of 9 red stamped BID SET SEP 22 1999 by J.M. Carden Sprinkler Co., Inc.

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Schedule 3 To Work Letter  
Preliminary Construction Schedule  
[To be Attached]

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CHAMPAGNE PRELIMINARY SCHEDULE  
FULLMER CONSTRUCTION.....11/4/99

					NOVEMBER	DECEMBER		JANUARY		FEBRUARY		MARCH		
					11/14	11/29	12/12	12/26	1/9	1/23	2/4	2/20	3/5	3/19
NO.	DURATION	START	FINISH	TASK NAME										
1	6 days	11/15/99	11/24/99	GRADING										
2	40 days	11/26/99	1/29/00	BLDG CONCRETE										
3	17 days	11/30/99	12/29/99	SEWER & STORM DRAIN										
4	10 days	12/21/99	1/2/00	FIRE AND WATER LINES										
5	10 days	1/4/00	1/17/00	EDISON & PHONE										
6	3 days	1/18/00	1/20/00	SLEEVES RIGHT OF WAY										
7	10 days	1/21/00	2/3/00	FOUR APPROACHES										
8	6 days	1/28/00	2/4/00	LIFT BUILDING & SCAN WALLS										
10	4 days	1/31/00	2/5/00	WELD										
11	4 days	1/31/00	2/3/00	SET COLUMNS										
13	4 days	2/2/00	2/7/00	WATER BLAST										
17	20 days	2/3/00	3/1/00	SACK-TRKWELL-GLASS- REST										
12	16 days	2/4/00	2/24/00	K-BRACE WORK										
14	20 days	2/4/00	3/2/00	ROOF STRUCTURE										
9	2 days	2/7/00	2/9/00	GROUT PANELS										
16	20 days	2/8/00	3/7/00	SITE CONCRETE										
??	25 days	2/11/00	3/18/00	O. H. FIRE SPRINKLERS										
18	? days	2/18/00	2/28/00	PERIMETER CONDS/ DRAINS/B.FILL										
20	8 days	2/23/00	3/1/00	BUILD & LITE CURBS										
23	2 days	3/2/00	3/3/00	H2O RINSE BUILDING										
26	3 days	3/2/00	3/6/00	ROOF SHEET METAL										
16	3 days	3/3/00	3/6/99	FULL BRACES										
2?	10 days	3/6/00	3/7/00	FOURSTRIP										





GEAR

38 11 days 3/18/00 3/30/00 BUILD ELECT  
ROOM

46 2 days 3/17/00 3/28/00 FINAL GRADE  
WALKS 1ST

22 10 days 3/20/00 3/31/00 DOCK  
EQUIPMENT

27 18 days 3/20/00 4/7/00 ROLL-UP  
DOORS

28 4 days 3/20/00 3/23/00 EXT. MAN  
DOORS

44 6 days 3/20/00 3/27/00 WALKS & MAN  
DR. PADS

60 2 days 3/24/00 3/23/00 CLEAN & REAL  
FLOOR

36 12 days 3/24/00 4/10/00 HI-BAY LITES

83 2 days 3/24/00 3/31/00 BASE & PAVE  
P.LOT

32 7 days 3/30/00 4/7/00 SKYLITES

33 8 days 3/30/00 4/8/00 ROOF EXHAUST  
UNITS

41 1 day 3/30/00 3/30/00 CAULK  
SCUPPERS

43 3 days 3/31/00 4/4/00 DOWNSPOUTS

47 1 day 3/31/00 3/31/00 EDISON/GTE  
ENERGIZED

38 8 days 3/31/00 3/31/00 RACKS BEGIN  
IF CITY  
"OK"(S)

49 8 days 4/2/00 4/12/00 FENCE &  
GATES

51 2 days 4/3/00 4/12/00 STRIPE P.LOT

88 20 days 4/4/00 6/1/00 LANDSCAPE

38 2 days 4/5/00 4/8/00 HAND RAILS &  
TRASH  
GATES

64 8 days 4/16/00 4/17/00 FINISH EXT.  
BLDG.  
PAINT

65 10 days 5/2/00 5/15/00 BLDG. FINALS

29 0 days 5/16/00 5/16/00 JOB COMPLETE

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EXHIBIT B  
PROTECTED LESSEE OWNED ALTERATIONS  
[TO BE LISTED BY LESSEE AND ATTACHED]

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EXHIBIT B  
PROTECTED LESSEE OWNED ALTERATIONS

Material Handling system whose components include, but are not limited to, the following:

A tilt tray sorter, conveyor (consisting of, among other things, certain mechanical equipment, spiral chutes, spiral declines and truck loaders), platforms and pick modules (which platforms and pick modules consist of, among other things, a main platform, induction platforms, level modules, shelving, fire protection, lighting and footings), case sealers, in-line scales and auto-tie bailers

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ADDENDUM  
[TO BE ATTACHED]

ADDENDUM TO INDUSTRIAL/COMMERCIAL  
SINGLE-TENANT LEASE - NET

LESSOR: Champagne Building Group, LP, a California limited partnership  
LESSEE: Skechers USA, Inc., a California Corporation  
LEASE DATED: October 15, 1999

The following provisions are added to that certain Standard Industrial/Commercial Single-Tenant Lease-Net dated for reference purposes as of October 15, 1999, by and between Champagne Building Group LP, a California limited partnership, as Lessor, and Skechers, USA, Inc., a California Corporation, as Lessee. In the event of any conflict between the terms of the Printed Lease and this Addendum, the terms of this Addendum shall control.

50. Rent: For the first sixty (60) months of the original term of the lease the Base Rent is \$85,693.00 net per month. Beginning on the sixty-first (61st) month and continuing until the eighty-fourth (84th) month, the Base Rent shall be \$92,285.00 net per month.

51. [intentionally omitted]

52. Option to Extend Term: Lessee shall have one option (the "Option") to extend the Term of the Lease for a period of five (5) years (hereafter the "Option Period"), provided that all of the following conditions are satisfied: (a) Lessee shall provide Lessor with written notice (the "Option Exercise Notice") of Lessee's election to exercise the Option not less than one hundred eighty (180) nor more than three hundred sixty (360) days prior to the expiration of the Original Term of the Lease, and (b) no default by Lessee of its obligations under this Lease shall have occurred and be continuing, either at the time Lessee delivers the Option Exercise Notice to Lessor or at the commencement of the Option Period. The Base Rent for Option Period shall be equal to ninety-five percent (95%) of the Fair market Rental Value (as defined below) for comparable industrial buildings in the City of Ontario, but in no event shall the monthly Base Rent for Option Period be less than the monthly Base Rent for the last month of the Original Term.

52.1 Upon receipt by Lessor of an Option Exercise Notice, Lessor and Lessee shall confer and attempt to agree upon the initial monthly Base Rent for the Option Period. If such an agreement is not reached within thirty (30) days following the receipt of such notice by Lessor, then Fair Market Rental Value ("FMRV") for the Premises shall be determined as provided in Paragraph 52.2 below.

52.2 To determine FMRV, Lessor shall engage at its sole cost and expense a MAI certified appraiser ("Lessor's Appraiser") who shall render a written opinion of the FMRV for the Premises ("Lessor's FMRV"). Lessee shall have five (5) business days to accept or reject Lessor's FMRV. If Lessee accepts Lessor's FMRV, Lessee shall reimburse Lessor for one-half of the fees and expenses of Lessor's Appraiser. If Lessee rejects such determination of FMRV, Lessee shall engage at its sole cost and expense a second Independent MAI certified appraiser ("Lessee's Appraiser") who shall also render a written opinion of the FMRV for the Premises ("Lessee's FMRV"). If Lessor's FMRV is less than 10% greater or less than Lessee's FMRV, then the FMRV for the Premises shall be the average of Lessor's FMRV and Lessee's FMRV. If the difference

between Lessor's FMRV and Lessee's FMRV is 10% or more, and Lessor and Lessee cannot agree between themselves as to the FMRV for the Premises, then FMRV shall be determined by a third independent MAI certified appraiser (the "Third Appraiser") mutually selected by Lessor's Appraiser and Lessee's Appraiser; provided, however, in no event will the FMRV be less than the lowest of Lessor's

FMRV and Lessee's FMRV nor higher than the highest of Lessor's FMRV and Lessee's FMRV. The Third Appraiser shall render a written opinion of the FMRV for the Premises, which shall be binding and conclusive upon Lessor and Lessee. The costs of the Third Appraiser shall be shared equally by Lessor and Lessee.

Except for the option to extend the term of the Lease for one (1), five (5) year period as provided in this Paragraph 52, Lessee shall have no other option to extend the term of the Lease, or option to purchase, option to lease or right of first refusal.

53. Premises Total Destruction. The following language replaces the language contained in Paragraph 9.1(b) of the Lease:

"(b) "Premises Total Destruction" shall mean damage or destruction to improvements on the Premises, other than Lessee Owned Alterations and Utility Installations and Trade Fixtures, which cannot reasonably be repaired within six (6) months or less from the date of the damage or destruction. Within thirty (30) days following the date of the damage or destruction, Lessor shall select a general contractor ("Lessor's Contractor") who shall, by written notice to Lessor and Lessee (a "Determination Notice"), determine whether or not the repair of such damage or destruction can be completed within six (6) months from the date of the damage or destruction. If Lessee elects not to accept such determination by Lessor's Contractor, Lessee shall, at Lessee's sole expense, select another general contractor ("Lessee's Contractor") who shall, within ten (10) days after receipt by Lessee of such Determination Notice, by written notice to Lessor and Lessee, determine whether or not the repair of such damage or destruction can be completed within six (6) months from the date of the damage or destruction. Should Lessor's Contractor and Lessee's Contractor fail to agree upon whether such damage or destruction can be repaired within six (6) months from the date of the damage or destruction, then the matter shall be resolved by binding arbitration in accordance with the Rules of the American Arbitration Association."

54. Partial Damage-Uninsured Loss. The following language replaces the first two sentences of Paragraph 9.3 of the Lease:

"If a Premises Partial Damage occurs that is not an Insured Loss, unless caused by a negligent or willful act of Lessee (in which event Lessee shall make the repairs at Lessee's expense), (i) if the total cost of repairing such damage is reasonably determined by an impartial general contractor selected by Lessor to be equal to or less than \$250,000, then Lessor shall repair such damage (but not Lessee's Trade Fixtures or Lessee Owned Alterations and/or Utility Installations), and (ii) if the total cost of repairing such damage is reasonably determined by an impartial general contractor selected by Lessor to be greater than \$250,000, then Lessor may either (A) repair such damage (but not Lessee's Trade Fixtures or Lessee Owned Alterations and/or Utility Installations) as soon as is reasonably possible at Lessor's expense, in which event the Lease shall remain in full force and effect, or (B) terminate the Lease by giving written notice to Lessee (a

"Termination Notice") within thirty (30) days after the date that Lessor becomes aware of the occurrence of such damage, such termination to be effective one hundred twenty (120) days after the date of such notice; provided, however, that the Lease shall not so terminate if Lessee, by written notice to Lessor within thirty (30) days after receipt of such Termination Notice, elects to repair such damage (after Lessor's payment of the foregoing \$250,000 sum) at Lessee's sole expense."

55. Damage Near End of Term. The following language replaces the language

contained in the first sentence of Paragraph 9.5 of the Lease:

"If at any time during the last six (6) months of the Original Term (as the same may be extended) there is damage to the Premises for which the cost of repairs is reasonably estimated by an impartial general contractor selected by Lessor to exceed one-month's then Base Rent, whether or not an Insured Loss, Lessor or Lessee may, by written notice to the other party within thirty (30) days after the date of occurrence of such damage, terminate this Lease effective sixty (60) days following the date of occurrence of such damage."

56. Assignment and Subletting-Lessor's Consent Required. The following language is added as a new Paragraph 12.1(b) of the Lease:

"(b) Lessee shall have the right, without Lessor's consent but after prior notice to Lessor including the name, address and contact information of such assignee, to assign the Lease to an entity (an "Affiliate") controlling, under common control with, or controlled by Lessee, including an entity resulting from a merger or consolidation by Lessee, provided that the Affiliate assumes in writing Lessee's obligations under this Lease in the proportion that the number of square feet of the Premises transferred to the Affiliate of Lessee bears to the total number of square feet in the Premises, without relieving Lessee of any liability under the Lease. Any such Affiliate assignee shall be deemed to have assumed all liabilities of Lessee hereunder. Lessee or such Affiliate assignee shall provide such additional information relating to such Affiliate assigned as Lessor shall request from time to time."

57. Condemnation. The following language is inserted after the third sentence of Paragraph 14 of the Lease:

"Condemnation awards and/or payments shall be the property of Lessor, whether such award shall be compensation for diminution in value of the Premises, the value of the part taken, or for severance damages; provided, however, that Lessee shall be entitled to any portion of such condemnation award specifically attributable to (i) Lessee's loss of business goodwill and/or Trade Fixtures, and (ii) if this Lease is terminated pursuant to the provisions of Paragraph 14 of the Lease, Lessee's reasonable relocation expenses and any excess of the market value of the Premises for the remainder of the Original Term (as the same may be extended) over the present value as of the date of such termination of the Base Rent payable for the remainder of the Original Term (as the same may be extended)."

58. Lessor's Access; Showing Premises; Repairs. The following language replaces the language contained in Paragraph 32 of the Lease:

"Lessor and Lessor's agents shall have the right to enter the Premises at any time, in the case of an emergency, and otherwise, upon 24 hours' prior notice to Lessee, for the purpose of showing same to prospective purchasers, lenders, or lessees, and making alterations, repairs, improvements and additions to the Premises as Lessor may deem necessary. All such activities shall be without abatement of rent or liability to Lessor. Lessor may at any time place one commercially standard, free-standing "For Sale" sign at a location to be selected by mutual agreement of Lessor and Lessee near the perimeter of the Premises. Lessor may at any time during the last six (6) months of the Original Term (as the same may be extended) place one commercially standard, free-standing "For Lease" sign at a location to be selected by Lessor near the perimeter of the Premises. Lessee may at any time place one commercially standard, free-standing "For Sublease" sign at a location to be selected by Lessee near the perimeter of the Premises."

59. Substantial Completion. For purposes of determining the Commencement Date under Paragraph 1.3 of the Lease, "Substantial Completion" shall mean and refer to the following:

"Substantial Completion" shall mean that point in time when Landlord's architect certifies that construction of the Base Building is substantially complete in accordance with the Work Letter so that Tenant can legally occupy and utilize the Premises in accordance with City laws and regulations. Tenant acknowledges that Tenant will be constructing Tenant Improvements, including without limitation, racking and material handling system pursuant to a separate permit from the City and in accordance with the Work Letter. "Substantial Completion" shall have occurred upon the satisfaction of the conditions of the first sentence of this Section whether or not Tenant shall have completed its Tenant Improvements."

60 Connection to Neighboring Property. Tenant currently occupies, itself or through one or more Affiliates, facilities on properties that are adjacent to the Premises. Tenant has expressed its desire to connect its material handling system from the Premises to such adjacent facilities. Landlord consents to the connection of such systems, and will cooperate with Tenant in establishing such connection (including, without limitation, the performance of any reasonable acts or the execution of any reasonable documents acknowledging such Landlord consent), provided, however, that Tenant is solely responsible (i) for any and all expenses related to and (ii) for obtaining all permissions and consents, from governmental entities as well as adjacent property owners, necessary to permit such connections to be lawfully made. Tenant agrees to indemnify and hold Landlord harmless from and against any and all liability, loss, cost or damage arising out of the construction, installation and maintenance of any facilities for the connection of such systems. THIS LEASE IS NOT CONDITIONED IN ANY WAY UPON TENANT OBTAINING SUCH PERMISSIONS AND CONSENTS.

61 Delay in Commencement Date. Landlord agrees to use its best commercially reasonable efforts to cause Substantial Completion to have occurred on or before the Scheduled Commencement Date. If, despite said efforts, and subject to extension of the Scheduled Completion Date on account of Delays Caused by Tenant and Force Majeure Delays (both as hereinafter defined) and subject to Tenant's obligation to mitigate its damages,

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Substantial Completion has not occurred prior to the Scheduled Commencement Date, Landlord shall indemnify and hold Tenant harmless for Tenant's actual expenses and damages incurred as a result of Substantial Completion being delayed beyond the Scheduled Commencement Date; PROVIDED, HOWEVER, IN NO EVENT SHALL THE TOTAL OF DAMAGES PAYABLE FROM LANDLORD TO TENANT EXCEED \$2,600 FOR EACH DAY SUBSTANTIAL COMPLETION IS DELAYED BEYOND THE SCHEDULED COMPLETION DATE (AS EXTENDED) OR \$156,000 IN TOTAL. In the event Landlord fails to reimburse Tenant as herein set forth, then among the other remedies available to Tenant, Tenant shall have the right to offset its expenses, damages, losses and liabilities against Base Rent.

62. Delays Caused by Tenant. "Delays Caused by Tenant" shall mean any actual delay in the Substantial Completion of the Base Building, caused by an act or omission of Tenant, its agents or contractors in performing Tenant's obligations under the Lease, including, without limitation, the following:

- Interference by Tenant. Delays due to interference by Tenant, its agents or contractors with the completion of the Base Building; or
- Delays in Permits or Approvals. Delays in Landlord obtaining governmental approvals or permits due to the acts or omissions of Tenant, its agents or contractors, whether relating to the Tenant

Improvements or otherwise.

63. Force Majeure Delays. "Force Majeure Delay(s)" shall mean any actual delay due to: fire, earthquake, abnormal rains or other acts of God; acts of public enemy, war, rioting, insurrection, or other civil commotion; and strikes or boycotts or the unavailability or critical materials or workmen, which is or are beyond the reasonable control of Landlord or its contractors.
64. Extension of Scheduled Commencement Date. The Scheduled Commencement Date shall be extended one (1) day for each day in which there is either a Delay Caused by Tenant or a Force Majeure Delay; provided, however, if the Scheduled Commencement Date is so extended by more than sixty (60) days, then Tenant may elect to terminate this Lease upon ten (10) days notice to Landlord unless the Scheduled Commencement Date occurs prior to the end of such ten (10) day period, in which latter event the Lease shall not terminate.
65. Tenant Obligation to Mitigate. In the event that the Commencement Date has not occurred on or before the Scheduled Commencement Date, as extended, Tenant shall make a good faith effort to reasonably mitigate its damages. Tenants reasonable costs of mitigation shall be included within the actual expenses and damages for which Landlord has agreed to indemnify Tenant pursuant to Paragraph 61 of this Addendum. Without limiting the generality of the obligation to mitigate its damages, at a minimum, Tenant agrees to use commercially reasonable efforts: (i) to attempt to extend its current rights to remain in its current premises at 5725 East Jurupa Street, City of Ontario, California (the "Current Premises"); (ii) to holdover in the Current Premises under the provisions, if any, of the current lease therefor; and/or (iii) to delay its subtenant in taking occupancy of the

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Current Premises. Under no circumstances shall Tenant be required to commence any legal proceedings in connection with such mitigation efforts.

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#### Mediation Addendum

MEDIATION OF DISPUTES: LANDLORD AND TENANT AGREE TO MEDIATE ANY DISPUTE OR CLAIM BETWEEN THEM ARISING OUT OF THIS LEASE (AND WORK LETTER) BEFORE RESORTING TO ARBITRATION OR COURT ACTION. Mediation is a process in which parties attempt to resolve a dispute by submitting it to an impartial, neutral mediator who is authorized to facilitate the resolution of the dispute but who is not empowered to impose a settlement on the parties. Mediation fees, if any, shall be divided equally among the parties involved. Before the mediation begins, the parties agree to sign a document limiting the admissibility in arbitration or any civil action of anything said, any admission made, and any documents prepared, in the course of the mediation, consistent with Evidence Code Section 1119. IF ANY PARTY COMMENCES AN ARBITRATION OR COURT ACTION BASED ON A DISPUTE OR CLAIM TO WHICH THIS PARAGRAPH APPLIES WITHOUT FIRST ATTEMPTING TO RESOLVE THE MATTER THROUGH MEDIATION, THEN IN THE DISCRETION OF THE ARBITRATOR(S) OR JUDGE, THAT PARTY SHALL NOT BE ENTITLED TO RECOVER ATTORNEY'S FEES EVEN IF THEY WOULD OTHERWISE BE AVAILABLE TO THAT PARTY IN ANY SUCH ARBITRATION OR COURT ACTION. However, the filing of a judicial action to enable the recording of a notice of pending action, for order of attachment, receivership, injunction, or other provisional remedies, shall not in itself constitute a loss of the right to recover attorney's fees under this provision. The following matters are excluded

from the requirement of mediation hereunder: (a) an unlawful detainer action, (b) the filing or enforcement of a mechanic's lien, and (c) any matter which is within the jurisdiction of a probate court.

/s/ [Signature Illegible]  
-----  
Lessor's Initial

/s/ [Signature Illegible]  
-----  
Lessee's Initials

STANDARD OFFICE LEASE -- GROSS  
AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION

Basic Lease Provisions ("Basic Lease Provisions")

1.1 PARTIES: This Lease, dated, for reference purposes only, November 18, 1999, is made by and between Pacifica California/Apollo, LLC (herein called "Lessor") and Skechers USA, Inc., doing business under the name of Skechers USA, Inc., (herein called "Lessee").

1.2 PREMISES: Suite Numbers(s) 125, 300, 320 floors, consisting of approximately 15,013 feet more or less, as defined, in paragraph 2 and shown on Exhibit "A" hereto (the "Premises").

1.3 BUILDING: Commonly described as being located at 225 S. Sepulveda Boulevard in the City of Manhattan Beach, County of Los Angeles, State of California, as more particularly described in Exhibit A hereto, and as defined in paragraph 2.

1.4 USE: General Office, subject to paragraph 6.

1.5 TERM: Sixty-four (64) months commencing March 1, 2000. See addendum ("Commencement Date") and ending May 1, 2005 as defined in paragraph 3. See addendum.

1.6 BASE RENT: \$36,031.20 per month, payable on the 1st day of each month, per paragraph 1.

1.7 BASE RENT INCREASE: On January 2, 2001 the monthly Base Rent payable under paragraph 1.6 above shall be adjusted as provided in paragraph 4.3 below.

1.8 RENT PAID UPON EXECUTION: \$36,031.20 for 1st months rent.

1.9 SECURITY DEPOSIT: \$5000.00.

1.10 LESSEE'S SHARE OF OPERATING EXPENSE INCREASE: 23.7% as defined in paragraph 4.2.

2. PREMISES, PARKING AND COMMON AREAS.

2.1 PREMISES: The Premises are a portion of a building, herein sometimes referred to as the "Building" identified in paragraph 1.3 of the Basic Lease Provisions. "Building" shall include adjacent parking structures used in connection therewith. The Premises, the Building, the Common Areas, the land upon which the same are located, along with all other buildings and improvements thereon or thereunder, are herein collectively referred to as the "Office Building Project." Lessor hereby leases to Lessee and Lessee leases from Lessor for the term, at the rental, and upon all of the conditions set forth herein, the real property referred to in the Basic Lease Provisions, paragraph 1.2, as the "Premises", including rights to the Common Areas as hereinafter specified.

2.2 VEHICLE PARKING: So long as Lessee is not in default, and subject to the rules and regulations attached hereto, and as established by Lessor from time to time, Lessee shall be entitled to rent and use See Addendum \_\_\_\_\_ parking spaces in the Office Building Project at the monthly rate applicable from time to time for monthly parking as set by Lessor and/or its licensee.

2.2.1 If Lessee commits, permits or allows any of the prohibited



activities described in the Lease or the rules then in effect, then Lessor shall have the right, without notice, in addition to such other rights and remedies that it may have, to remove or tow away the vehicle involved and charge the cost to Lessee, which cost shall be immediately payable upon demand by Lessor.

2.2.2 The monthly parking rate per parking space will be \$ See Addendum \_\_\_\_\_ per month at the commencement of the term of this Lease, and is subject to change upon five (5) days prior written notice to Lessee. Monthly parking fees shall be payable one month in advance prior to the first day of each calendar month.

2.3 COMMON AREAS -- DEFINITION. The term "Common Areas" is defined as all areas and facilities outside the Premises and within the exterior boundary line of the Office Building Project that are provided and designated by the Lessor from time to time for the general non-exclusive use of Lessor, Lessee and of other lessees of the Office Building Project and their respective employees, suppliers, shippers, customers and invitees, including but not limited to common entrances, lobbies, corridors, stairways and stairwells, public restrooms, elevators, escalators, parking areas to the extent not otherwise prohibited by the Lease, loading and unloading areas, trash areas, roadways, sidewalks, walkways, parkways, ramps, driveways, landscaped areas and decorative walls.

2.4 COMMON AREAS -- RULES AND REGULATIONS. Lessee agrees to abide by and conform to the rules and regulations attached hereto as Exhibit B with respect to the Office Building Project and Common Areas, and to cause its employees, suppliers, shippers, customers, and invitees to so abide and conform. Lessor or such other person(s) as Lessor may appoint shall have the exclusive control and management of the Common Areas and shall have the right, from time to time, to modify, amend and enforce said rules and regulations. Lessor shall not be responsible to Lessee for the non-compliance with said rules and regulations by other lessees, their agents, employees and invitees of the Office Building Project.

2.5 COMMON AREAS -- CHANGES. Lessor shall have the right, in Lessor's sole discretion, from time to time:

(a) To make changes to the Building interior and exterior and Common Areas, including, without limitation, changes in the location, size shape, number, and appearance thereof, including but not limited to the lobbies, windows, stairways, air shafts, elevators, escalators, restrooms, driveways, entrances, parking spaces, parking areas, loading and unloading areas, ingress, egress, direction of traffic, decorative walls, landscaped areas and walkways; provided, however, Lessor shall at all times provide the parking facilities required by applicable law; [Illegible]

(b) [Illegible]

(c) [Illegible] that such other and improvements have a reasonable and functional relationship to the Office Building Project;

(d) To add additional buildings and improvements to the Common Areas;

(e) To use the Common Areas while engaged in making additional improvements, repairs or alterations to the Office Building Project, or any portion thereof;

(f) To do and perform such other acts and make such other changes in, to or with respect to the Common Areas and Office Building Project as Lessor may, in the exercise of sound business judgment deem to be appropriate.

### 3. TERM.

3.1 TERM. The term and Commencement Date of this Lease shall be as specified in paragraph 1.5 of the Basic Lease Provisions.

3.2 DELAY POSSESSION. Notwithstanding said Commencement Date, if for any reason Lessor cannot deliver possession of the Premises to Lessee on said date

and subject to paragraph 3.2.2, Lessor shall not be subject to any liability therefor, nor shall such failure affect the validity of this Lease or the obligations of Lessee hereunder or extend the term hereof; but in such case, Lessee shall not be obligated to pay rent or perform any other obligation or

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FULL SERVICE-GROSS  
REVISED  
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Lease under the terms of this Lease, except as may be otherwise provided in this Lease, until possession of the Premises is tendered to Lessee as hereinafter defined; provided, however, that if Lessor shall not have delivered possession of the Premises within sixty (60) days following said Commencement Date as the same may be extended under the terms of a Work Letter executed by Lessor and Lessee. Lessee may, at Lessee's option, by notice in writing to Lessor within ten (10) days thereafter, cancel this Lease, in which event the parties shall be discharged from all obligations hereunder, provided, however, that, as to Lessee's obligations, Lessee first reimburses Lessor for all costs incurred for Non-Standard Improvements and, as to Lessor's obligations, Lessor shall return any money previously deposited by Lessee (less any offsets due Lessor for Non-Standard Improvements), and provides further, that if such written notice by Lessee is not received by Lessor within said ten (10) day period, Lessee's right to cancel this Lease hereunder shall terminate and be of no further force or effect.

3.2.1 POSSESSION TENDERED - DEFINED. Possession of the Premises shall be deemed tendered to Lessee ("Tender of Possession") when (1) the improvements to be provided by Lessor under this Lease are substantially completed, (2) the Building utilities are ready to use in the Premises, (3) Lessee has reasonable access to the Premises, and (4) ten (10) days shall have expired following advance written notice to Lessee of the occurrence of the matters described in (1), (2) and (3), above of this paragraph 3.2.1.

3.2.2 DELAY CAUSED BY LESSEE. There shall be no abatement of rent, and the sixty (60) day period following the Commencement Date before which Lessee's right to cancel this Lease accrues under paragraph 3.2, shall be deemed extended to the extent of any delays caused by acts or omissions of Lessee, Lessee's agents, employees and contractors.

3.3 EARLY POSSESSION. If Lessee occupies the Premises prior to said Commencement Date, such occupancy shall be subject to all provisions of this Lease, such occupancy shall not change the termination date, and Lessee shall pay rent for such occupancy.

3.4 UNCERTAIN COMMENCEMENT. In the event commencement of the Lease term is defined as the completion of the improvements, Lessee and Lessor shall execute an amendment to this Lease establishing the date of Tender of Possession (as defined in paragraph 3.2.1) or the actual taking of possession by Lessee whichever first occurs, as the Commencement Date.

#### 4. RENT.

4.1 BASE RENT. Subject to adjustment as hereinafter provided in paragraph 4.3, and except as may be otherwise expressly provided in this Lease, Lessee shall pay to Lessor the Base Rent for the Premises set forth in paragraph 1.6 of the Basic Lease Provisions, without offset or deduction. Lessee shall pay Lessor upon execution hereof the advance Base Rent described in paragraph 1.8

of the Basic Lease Provisions. Rent for any period during the term hereof which is for less than one month shall be prorated based upon the actual number of days of the calendar month involved. Rent shall be payable in lawful money of the United States to Lessor at the address stated herein or to such other persons or at such other places as Lessor may designate in writing.

4.2 OPERATING EXPENSE INCREASE. Lessee shall pay to Lessor during the term hereof, in addition to the Base Rent, Lessee's Share, as hereinafter defined, of the amount by which all Operating Expenses, as hereinafter defined, for each Comparison Year exceeds the amount of all Operating Expenses for the Base Year, such access being hereinafter referred to as the "Operating Expense Increase", in accordance with the following provisions:

(a) "Lessee's Share" is defined, for purposes of this Lease, as the percentage set forth in paragraph 1.10 of the Basic Lease Provisions, which percentage has been determined by dividing the approximate square footage of the Premises by the total approximate square footage of the rentable space contained in the Office Building Project. It is understood and agreed that the square footage figures set forth in the Basic Lease Provisions are approximations which Lessor and Lessee agree are reasonable and shall not be subject to revision except in connection with an actual change in the size of the Premises or a change in the space available for lease in the Office Building Project.

(b) "Base Year" is defined as the calendar year in which the Lease term commences.

(c) "Comparison Year" is defined as each calendar year during the term of this Lease subsequent to the Base Year; provided, however, Lessee shall have no obligation to pay a share of the Operating Expense Increase applicable to the first twelve (12) months of the Lease Term (other than such as are mandated by a governmental authority, as to which government mandated expenses Lessee shall pay Lessee's Share, notwithstanding they occur during the first twelve (12) months). Lessee's Share of the Operating Expense Increase for the first and last Comparison Years of the Lease Term shall be prorated according to that portion of such Comparison Year as to which Lessee is responsible for a share of such increase. Operating expenses shall be adjusted to reflect a ninety-five (95%) level of occupancy.

(d) "Operating Expenses" is defined, for purposes of this Lease, to include all costs, if any, incurred by Lessor in the exercise of its reasonable discretion, for:

(i) The operation, repair, maintenance, and replacement, in neat, clean, safe, good order and condition, of the Office Building Project including but not limited to, the following:

(a) The Common Areas, including their surfaces, coverings, decorative items, carpets, drapes and window coverings, and including parking areas, loading and unloading areas, trash areas, roadways, sidewalks, walkways, stairways, parkways, driveways, landscaped areas, striping bumpers, irrigation systems, Common Area lighting facilities, building exteriors and roofs, fences and gates;

(b) All heating, air conditioning, plumbing, electrical systems, life safety equipment, telecommunication and other equipment used in common by, or for the benefit of, lessees or occupants of the Office Building Project, including elevators and escalators, tenant directories, fire detection systems including sprinkler system maintenance and repair.

(ii) Trash disposal, janitorial and security services;

(iii) Any other service to be provided by Lessor that is elsewhere in this Lease stated to be an "Operating Expense";

(iv) The cost of the premiums for the liability and property insurance policies to be maintained by Lessor under paragraph 8 hereof;

(v) The amount of the real property taxes to be paid by Lessor under paragraph 10.1 hereof;

(vi) The cost of water, sewer, gas, electricity, and other publicly mandated services to the Office Building Project;

(vii) Labor, salaries, and applicable fringe benefits and costs, materials, supplies and tools, used in maintaining and/or cleaning the Office Building Project and accounting and a management fee attributable to the operation of the Office Building Project;

(viii) Replacing and/or adding improvements mandated by any governmental agency and any repairs or removals necessitated thereby amortized over its useful life according to Federal income tax regulations or guidelines for depreciation thereof (including interest on the unamortized balance as is then reasonable in the judgment of Lessor's accountants);

(ix) Replacement of equipment or improvements that have a useful life for depreciation purposes according to Federal income tax guidelines of five (5) years or less as amortized over such life;

(e) Operating Expenses shall not include the costs of replacements of equipment or improvements that have a useful life for Federal income tax purposes in excess of five (5) years unless it is of the type described in paragraph 4.2(d) (viii), in which case their cost shall be included as above provided.

(f) Operating Expenses shall not include any expenses paid by any lessee directly to third parties, or as to which Lessor is otherwise reimbursed by any third party, other tenant, or by insurance proceeds.

(g) Lessee's Share of Operating Expense Increase shall be payable by Lessee within ten (10) days after a reasonably detailed statement of actual expenses is presented to Lessee by Lessor. At Lessor's option, however, an amount may be estimated by Lessor from time to time in advance of Lessee's Share of ?????? Expense Increase for any Commission Year, and the same shall be payable monthly [Illegible]

Year a reasonably detailed statement showing Lessee's Share of the actual Operating Expense Increase incurred during such year. If Lessee's payments under this paragraph 4.2(g) during said Comparison Year exceed Lessee's Share as indicated on said statement, Lessee shall be entitled to credit the amount of such overpayment against Lessee's Share of Operating Expense Increase next falling due. If Lessee's payments under this paragraph during said Comparison Year were less than Lessee's Share as indicated on said statement, Lessee shall pay to Lessor the amount of the deficiency within ten (10) days after delivery by Lessor to Lessee of said statement. Lessor and Lessee shall forthwith adjust between them by cash payment any balance determined to exist with respect to that portion of the last Comparison Year for which Lessee is responsible as to Operating Expense Increases, notwithstanding that the Lease term may have terminated before the end of such Comparison Year.

5. SECURITY DEPOSIT. Lessee shall deposit with Lessor upon execution hereof the security deposit set forth in paragraph 1.9 of the Basic Lease Provisions as security for Lessee's faithful performance of Lessee's obligations hereunder. If Lessee fails to pay rent or other charges due hereunder, or otherwise defaults with respect to any provision of this Lease, Lessor may use, apply or retain all or any portion of said deposit for the payment of any rent or other charge in default for the payment of any other sum to which Lessor may become obligated by reason of Lessee's default, or to compensate Lessor for any loss or damage which Lessor may suffer hereby. If Lessor so uses or applies all or any portion of said deposit, Lessee shall within ten (10) days after written

demand therefor deposit cash with Lessor in an amount sufficient to restore said deposit to the full amount then required of Lessee. If the monthly Base Rent shall, from time to time, increase during the term of this Lease, Lessee shall, at the time of such increase, deposit with Lessor additional money as a security deposit so that the total amount of the security deposit held by Lessor shall at all times bear the same proportion to the then current Base Rent as the initial security deposit bears to the initial Base Rent set forth in paragraph 1.6 of the Basic Lease Provisions. Lessor shall not be required to keep said security deposit separate from its general accounts. If Lessee performs all of Lessee's obligations hereunder, said deposit, or so much thereof as has not heretofore been applied by Lessor, shall be returned, without payment of interest or other increment for its use, to Lessee (or, at Lessor's option, to the last assignee, if any, of Lessee's interest hereunder) at the expiration of the term hereof, and after Lessee has vacated the Premises. No trust relationship is created herein between Lessor and Lessee with respect to said Security Deposit.

6. USE.

6.1 USE. The Premises shall be used and occupied only for the purpose set forth in paragraph 1.4 of the Basic Lease Provisions or any other use which is reasonably comparable to that use and for no other purpose.

6.2 COMPLIANCE WITH LAW.

(a) Lessor warrants to Lessee that the Premises, in the state existing on the date that the Lease term commences, but without regard to alterations or improvements made by Lessee or the use for which Lessee will occupy the Premises, does not violate any covenants or restrictions of record, or any applicable building code, regulation or ordinance in effect on such Lease term Commencement Date. In the event it is determined that this warranty has been violated, then it shall be the obligation of the Lessor, after written notice from Lessee, to promptly, at Lessor's sole cost and expense, rectify any such violation.

(b) Except as provided in paragraph 6.2(a) Lessee shall, at Lessee's expense, promptly comply with all applicable statutes, ordinances, rules, regulations, orders, covenants and restrictions of record, and requirements of any fire insurance underwriters or rating bureaus, now in effect or which may hereafter come into effect, whether or not they reflect a change in policy from that now existing, during the term or any part of the term hereof, relating in any manner to the Premises and the occupation and use by Lessee of the Premises. Lessee shall conduct its business in a lawful manner and shall not use or permit the use of the Premises or the Common Areas in any manner that will tend to create waste or a nuisance or shall tend to disturb other occupants of the Office Building Project.

6.3 CONDITION OF PREMISES.

(a) Lessor shall deliver the Premises to Lessee in a clean condition on the Lease Commencement Date (unless Lessee is already in possession) and Lessor warrants to Lessee that the plumbing, lighting, air conditioning, and hearing system in the Premises shall be in good operating condition. In the event that it is determined that this warranty has been violated, then it shall be the obligation of Lessor, after receipt of written notice from Lessee setting forth with specificity the nature of the violation, to promptly, at Lessor's sole cost, rectify such violation.

(b) Except as otherwise provided in this Lease, Lessee hereby accepts the Premises and the Office Building Project in their condition existing as of the Lease Commencement Date or the date that Lessee takes possession of the Premises, whichever is earlier, subject to all applicable zoning, municipal, county and state laws, ordinances and regulations governing and regulating the use of the Premises, and any easements, covenants or restrictions of record, and accepts this Lease subject thereto and to all matters disclosed thereby and by any exhibits attached hereto. Lessee acknowledges that it has satisfied itself by its own independent investigation that the Premises are suitable for its intended use, and that neither Lessor

nor Lessor's agent or agents has made any representation or warranty as to the present or future suitability of the Premises, Common Areas, or Office Building Project for the conduct of Lessee's business.

7. MAINTENANCE, REPAIRS, ALTERATIONS AND COMMON AREA SERVICES.

7.1 LESSOR'S OBLIGATIONS. Lessor also keeps the Office Building Project, including the Premises, interior and exterior walls, roof, and common areas, and the equipment whether used exclusively for the Premises or in common with other premises, in good condition and repair; provided, however, Lessor shall not be obligated to paint, repair or replace wall coverings, or to repair or replace any improvements that are not ordinarily a part of the Building or are above the Building standards. Except as provided in paragraph 9.5, there shall be no abatement of rent or liability of Lessee on account of any injury or interference with Lessee's business with respect to any improvements, alterations or repairs made by Lessor to the Office Building Project or any part thereof. Lessee expressly waives the benefits of any statute now or hereafter in effect which would otherwise afford Lessee the right to make repairs at Lessor's expense or to terminate this Lease because of Lessor's failure to keep the Premises in good order, condition or repair.

7.2 LESSEE'S OBLIGATIONS.

(a) Notwithstanding Lessor's obligation to keep the Premises in good condition and repair, Lessee shall be responsible for payment of the cost thereof to Lessor as additional rent for that portion of the cost of any maintenance and repair of the Premises, or any equipment (wherever located) that serves only Lessee or the Premises, to the extent such cost is attributable to causes beyond normal wear and tear. Lessee shall be responsible for the cost of painting, repairing or replacing wall coverings, and to repair or replace any Premises improvements that are not ordinarily a part of the Building or that ?? above than Building ?? Lessor may, at its option, upon reasonable notice, elect to have Lessee perform ?? such maintenance or ?? [CLIENT COPY ILLEGIBLE] received, ordinary wear and tear excepted, clean and free of debris. Any damage or deterioration of the Premises shall not be deemed ordinary wear and tear if the same could have been prevented by good maintenance practices by Lessee. Lessee shall repair any damage to the Premises occasioned by the installation or removal of Lessee's trade fixtures, alterations, furnishings and equipment. Except as otherwise stated in this Lease, Lessee shall leave the air lines, power panels, electrical distribution systems, lighting fixtures, air conditioning, window coverings, wall coverings, carpets, wall panelling, ceilings and plumbing on the Premises and in good operating condition.

7.3 ALTERATIONS AND ADDITIONS.

(a) Lessee shall not, without Lessor's prior written consent make any alterations, improvements, additions, Utility Installations or repairs in, on or about the Premises, or the Office Building Project. As used in this paragraph 7.3 the term "Utility Installation" shall mean carpeting, window and wall coverings, power panels, electrical distribution systems, lighting fixtures, air conditioning, plumbing, and telephone and telecommunication wiring and equipment. At the expiration of the term, Lessor may require the removal of any or all of said alterations, improvements, additions or Utility Installations, and the restoration of the Premises and the Office Building Project to their prior condition, at Lessee's expense. Should Lessor permit Lessee to make its own alterations, improvements, additions, or Utility Installations, Lessee shall use only such contractor as has been previously approved by Lessor, and Lessor may

acquire Lessee to provide Lessor, at Lessee's sole cost and expense, a lien and completion bond in an amount equal to one and one-half times the estimated asset of such improvements, to insure Lessor against any liability for mechanic's and materialmen's liens and to insure completion of the work. Should Lessee make any

alterations, improvements, additions or Utility Installations without the prior approval of Lessor, or use a contractor not expressly approved by Lessor, Lessor may, at any time during the term of this Lease, require that Lessee remove any part or all of the same.

(b) Any alterations, improvements, additions or Utility installations in or about the Premises or the Office Building Project that Lessee shall desire to make shall be presented to Lessor in written form, with proposed detailed plans. If Lessor shall give its consent to Lessee's making such alteration improvement, addition or Utility Installation, the consent shall be deemed conditioned upon Lessee acquiring a permit to do so from the applicable governmental agencies, furnishing a copy thereof to Lessor prior to the commencement of the work, and compliance by Lessee with all conditions of said permit in a prompt and expeditious manner.

(c) Lessee shall pay, when due, all claims for labor or materials furnished or alleged to have been furnished to or for Lessee at or for use in the premises, which claims are or may be secured by any mechanic's or materialmen's lien against the Premises, the Building or the Office Building Project, or any interest therein.

(d) Lessee shall give Lessor not less than ten (10) days' notice prior to the commencement of any work in the Premises by Lessee, and Lessor shall have the right to post notices of non-responsibility in or on the Premises or the Building as provided by law. If Lessee shall, in good faith, contest the validity of any such lien, claim or demand, then Lessee shall, at its sole expense defend itself and Lessor against the same and shall pay and satisfy any such adverse judgment that may be rendered thereon before the enforcement thereof against the Lessor or the Premise, the Building or the Office Building Project, upon the condition that if Lessor shall require, Lessee shall furnish to Lessor a surety bond satisfactory to Lessor in an amount equal to such contested lien claim or demand indemnifying Lessor against liability for the same and holding the Premises, the Building and the Office Building Project free from the effect of such lien or claim. In addition, Lessor may require Lessee to pay Lessor's reasonable attorneys fees and costs in participating in such action if Lessor shall decide it is to Lessor's interest so to do.

(e) All alterations, improvements, additions and Utility Installations (whether or not such Utility Installations constitute trade fixtures of Lessee), which may be made to the Premises by Lessee, including but not limited to, floor coverings, panelings, doors, drapes, built-ins, moldings, sound attenuation and lighting and telephone or communication systems, conduit, wiring and outlets, shall be made and done in a good and workmanlike manner and of good and sufficient quality and materials and shall be the property of Lessor and remain upon and be surrendered with the Premises at the expiration of the Lease term, unless Lessor requires their removal pursuant to paragraph 7.3(a). Provided Lessee is not in default, notwithstanding the provisions of this paragraph 7.3(e). Lessee's personal property and equipment, other than that which is affixed to the Premises so that it cannot be removed without material damage to the Premises or the Building, and other than Utility Installations, shall remain the property of Lessee and may be removed by Lessee subject to the provisions in paragraph 7.2.

(f) Lessee shall provide Lessor with as-built plans and specifications for any alterations, improvements, additions or Utility Installations.

7.4 Utility Additions. Lessor reserves the right to install new or additional utility facilities throughout the Office Building Project for the benefit of Lessor or Lessee, or any other lessee of the Office Building Project, including, but not by way of limitation, such utilities as plumbing, electrical systems, communication systems, and fire protection and detection systems, so long as such installations do not unreasonably interfere with Lessee's use of the Premises.

Insurance; Indemnity

8.1 Liability Insurance - Lessee. Lessee shall, at Lessee's expense,

obtain and keep in force during the term of this Lease a policy of Comprehensive General Liability insurance utilizing an Insurance Service Office standard form with Broad Form General Liability Endorsement (GL0404), or equivalent, in an amount of not less than \$1,000,000 per occurrence of bodily injury and property damage combined or in a greater amount as reasonably determined by Lessor and shall insure Lessee with Lessor as an additional insured against liability arising out of the use, occupancy or maintenance of the Premises. Compliance with the above requirement shall not, however, limit the liability of Lessee hereunder.

8.2 Liability Insurance - Lessor. Lessor shall obtain and keep in force during the term of this Lease a policy of Combined Single Limit Bodily injury and Broad Form Property Damage Insurance, plus coverage against such other risks Lessor deems advisable from time to time, insuring Lessor, but not Lessee, against liability arising out of the ownership, use, occupancy or maintenance of the Office Building Project in an amount not less than \$5,000,000.00 per occurrence.

8.3 Property Insurance - Lessee. Lessee shall, at Lessee's expense, obtain and keep in force during the term of this Lease for the benefit of Lessee, replacement cost fire and extended coverage insurance, with vandalism and malicious mischief, sprinkler leakage and earthquake sprinkler leakage endorsements, in an amount sufficient to cover not less than 100% of the full replacement cost, as the same may exist from time to time, of all of Lessee's personal property, fixtures, equipment and tenant improvements.

8.4 Property Insurance - Lessor. Lessor shall obtain and keep in force during the term of this Lease a policy or policies of insurance covering loss or damage to the Office Building Project improvements, but not Lessee's personal property, fixtures, equipment or tenant improvements, in the amount of the full replacement cost thereof, as the same may exist from time to time, utilizing Insurance Services Office standard form, or equivalent, providing protection against all perils included within the classification of fire, extended coverage, vandalism, malicious mischief, plate glass, and such other perils as Lessor deems advisable or may be required by a lender having a lien on the Office Building Project. In addition, Lessor shall obtain and keep in force, during the term of this Lease, a policy of rental value insurance covering a period of one year, with loss payable to Lessor, which insurance shall also cover all Operating Expenses for said period. Lessee will not be named in any such policies carried by Lessor and shall have no right to any proceeds therefrom. The policies required by these paragraphs 8.2 and 8.4 shall contain such deductibles as Lessor or the aforesaid lender may determine. In the event that the Premises shall suffer an insured loss as defined in paragraph 9.1(f) hereof, the deductible amounts under the applicable insurance policies shall be deemed an \_\_\_ rating Expense. Lessee shall not do or permit to be done anything which shall invalidate the insurance policies carried by Lessor. Lessee shall pay the entirety of any increase in the property insurance premium for the Office Building Project over what it was immediately prior to the commencement of the term at this Lease if the increase is specified by Lessor's insurance carrier as being caused by the nature of Lessee's occupancy or any act or omission of Lessee.

8.5 Insurance Policies. Lessee shall deliver to Lessor copies of liability insurance policies required under paragraph 8.1 or certificates evidencing the existence and amounts of such insurance within seven (7) days after the Commencement Date of this Lease. No such policy shall be cancelable or subject to reduction of coverage or other modification except after thirty (30) days prior written notice to Lessor. Lessee shall, at least thirty (30) days prior to the expiration of such policies, furnish Lessor with renewals thereof.

8.6 Waiver of Subrogation. Lessee and Lessor each hereby release and relieve the other, and waive their entire right of recovery against the other, the direct or consequential loss or damage arising out of or incident to the perils covered by property insurance carried by such party, whether due to the negligence of Lessor or Lessee or their agents, employees, contractors and/or invitees. If necessary all property insurance policies required under this Lease shall be endorsed to so provide.



8.7 Indemnity. Lessee shall indemnify and hold harmless Lessor and its agents, Lessor's master or ground lessor, partners and lenders, from and against any and all claims for damage to the person or property of anyone or any entity arising from Lessee's use of the Office Building Project or from the conduct of Lessee's

[ILLEGIBLE]

contractors, employees or invitees, and from and against all costs, attorney's fees, expenses and liabilities incurred by Lessor as the result of any such use, conduct, activity, work, things done, permitted or suffered, breach, default or negligence, and in dealing reasonably therewith, including but not limited to the defense or pursuit of any claim or any action or proceeding involved therein; and in case any action or proceeding be brought against Lessor by reason of any such matter, Lessee upon notice from Lessor shall defend the same at Lessee's expense by counsel reasonably satisfactory to Lessor and Lessor shall cooperate with Lessee in such defense. Lessor need not have first paid any such claim in order to be so indemnified. Lessee, as a material part of the consideration to Lessor, hereby assumes all risk of damage to property of Lessee or injury to persons, in, upon or about the Office Building Project arising from any cause and Lessee hereby waives all claims in respect thereof against Lessor.

8.8 Exemption of Lessor from Liability. Lessee hereby agrees that Lessor shall not be liable for injury to Lessee's business or any loss of income therefrom or for loss of or damage to the goods, wares, merchandise or other property of Lessee, Lessee's employees, invitees, customers, or any other person in or about the Premises or the Office Building Project, nor shall Lessor be liable for injury to the person of Lessee, Lessee's employees, agents or contractors, whether such damage or injury is caused by or results from theft, fire, steam, electricity, gas, water or rain, or from the breakage, leakage, construction or other defects of pipes, sprinklers, wires, appliances, plumbing, air conditioning or lighting fixtures, or from any other cause, whether said

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damage or injury results from conditions arising upon the Premises or upon other portions of the Office Building Project, or from other sources or places, or from new construction or the repair, alteration or improvement of any part of the Office Building Project, or of the equipment, fixtures or appurtenances applicable thereto, and regardless of whether the cause of such damage or injury or the means of repairing the same is inaccessible. Lessor shall not be liable for any damages arising from any act or neglect of any other lessee, occupant or user of the Office Building Project, nor from the failure of Lessor to enforce the provisions of any other lease of any other lessee of the Office Building Project.

8.9 NO REPRESENTATION OF ADEQUATE COVERAGE. Lessor makes no representation that the limits or forms of coverage of insurance specified in this paragraph 8 are adequate to cover Lessee's property or obligations under this Lease.

9. DAMAGE OR DESTRUCTION.

9.1 DEFINITIONS.

(a) "Premises Damage" shall mean if the Premises are damaged or destroyed to any extent.

(b) "Premises Building Partial Damage" shall mean if the Building of which the Premises are a part is damaged or destroyed to the extent that the cost to repair is less than fifty percent (50%) of the then Replacement Cost of the Building.

(c) "Premises Building Total Destruction" shall mean if the Building of which the Premises are a part is damaged or destroyed to the extent that the cost to repair is fifty percent (50%) or more of the then Replacement Cost of the Building.

(d) "Office Building Project Buildings" shall mean all of the buildings on the Office Building Project site.

(e) "Office Building Project Buildings Total Destruction" shall mean if the Office Building Project Buildings are damaged or destroyed to the extent that the cost to repair is fifty percent (50%) or more of the then Replacement Cost of the Office Building Project Buildings.

(f) "Insured Loss" shall mean damage or destruction which was caused by an event required to be covered by the insurance described in paragraph 8. The fact that an Insured Loss has a deductible amount shall not make the loss an uninsured loss.

(g) "Replacement Cost" shall mean the amount of money necessary to be spent in order to repair or rebuild the damaged area to the condition that existed immediately prior to the damage occurring, excluding all improvements made by lessees, other than those installed by Lessor at Lessee's expense.

## 9.2 PREMISES DAMAGE; PREMISES BUILDING PARTIAL DAMAGE.

(a) Insured Loss: Subject to the provisions of paragraphs 9.4 and 9.5, if at any time during the term of this Lease there is damage which is an Insured Loss and which falls into the classification of either Premises Damage or Premises Building Partial Damage, then Lessor shall, as soon as reasonably possible and to the extent the required materials and labor are readily available through usual commercial channels, at Lessor's expense, repair such damage (but not Lessee's fixtures, equipment or tenant improvements originally paid for by Lessee) to its condition existing at the time of the damage, and this Lease shall continue in full force and effect.

(b) Uninsured Loss: Subject to the provisions of paragraphs 9.4 and 9.5, if at any time during the term of this Lease there is damage which is not an Insured Loss and which falls within the classification of Premises Damage or Premises Building Partial Damage, unless caused by a negligent or willful act of Lessee (in which event Lessee shall make the repairs at Lessee's expense), which damage prevents Lessee from making any substantial use of the Premises, Lessor may at lessor's option either (i) repair such damage as soon as reasonably possible at Lessor's expense, in which event this Lease shall continue in full force and effect, or (ii) give written notice to Lessee within thirty (30) days after the date of the occurrence of such damage of Lessor's intention to cancel and terminate this Lease as of the date of the occurrence of such damage, in which event this Lease shall terminate as of the date of the occurrence of such damage.

9.3 PREMISES BUILDING TOTAL DESTRUCTION; OFFICE BUILDING PROJECT TOTAL DESTRUCTION. Subject to the provisions of paragraphs 9.4 and 9.5, if any time during the term of this Lease there is damage, whether or not it is an Insured Loss, which falls into the classifications of either (i) Premises Building Total Destruction, or (ii) Office Building Project Total Destruction, then Lessor may at Lessor's option either (i) repair such damage or destruction as soon as reasonably possible at Lessor's expense (to the extent the required materials are readily available through usual commercial channels) to its condition existing at the time of the damage, but not Lessee's fixtures, equipment or tenant improvements, and this Lease shall continue in full force and effect, or (ii) give written notice to Lessee within thirty (30) days after the date of occurrence of such damage of Lessor's intention to cancel and terminate this Lease, in which case this Lease shall terminate as of the date of the occurrence of such damage.

## 9.4 DAMAGE NEAR END OF TERM.

(a) Subject to paragraph 9.4(b), if at any time during the last twelve (12) months of the term of this Lease there is substantial damage to the Premises, Lessor may at Lessor's option cancel and terminate this Lease as of the date of occurrence of such damage by giving written notice to Lessee of Lessor's election to do so within 30 days after the date of occurrence of such damage.

(b) Notwithstanding paragraph 9.4(a), in the event that Lessee has an option to extend or renew this Lease, and the time within which said option may be exercised has not yet expired, Lessee shall exercise such option, if it is to be exercised at all, no later than twenty (20) days after the occurrence of an Insured Loss falling within the classification of Premises Damage during the last twelve (12) months of the term of this Lease. If Lessee duly exercises such option during said twenty (20) day period, Lessor shall, at Lessor's expense, repair such damage, but not Lessee's fixtures, equipment or tenant improvements, as soon as reasonably possible and this Lease shall continue in full force and effect. If Lessee fails to exercise such option during said twenty (20) day period, then Lessee may at Lessor's option terminate and cancel this Lease as of the expiration of said twenty (20) day period by giving written notice to Lessee of Lessor's election to do so within ten (10) days after the expiration of said twenty (20) day period, notwithstanding any term or provision in the grant of option to the contrary.

#### 9.5 ABATEMENT OF RENT; LESSEE'S REMEDIES.

(a) In the event Lessor repairs or restores the Building or Premises pursuant to the provisions of this paragraph 9, and any part of the Premises ??? not usable (including loss of use due to loss of access or essential services), the rent payable hereunder (including Lessee's Share of Operating Expense Increase) for the period during which such damage, repair or restoration continues shall be abated, provided (1) the damage was not result of the negligence of Lessee, and (2) such abatement shall only be to the extent the operation and profitability of Lessee's business as operated from the Premises is adversely affected. Except for said abatement of rent, if any, Lessee shall have no claim against Lessor for any damage suffered by reason of any such damage, destruction, repair or restoration.

(b) If Lessor shall be obligated to repair or restore the Premises or the Building under the provisions of this Paragraph 9 and shall not commence such repair or restoration within ninety (90) days after such occurrence, or if Lessor shall not complete the restoration and repair within six (6) months after such occurrence, Lessee may at Lessee's option cancel and terminate this Lease by giving Lessor written notice of Lessee's election to do so at any time prior to the commencement or completion, respectively, of such repair or restoration. In such event this Lease shall terminate as of the date of such notice.

(c) Lessee agrees to cooperate with Lessor in connection with any such restoration and repair, including but not limited to the approval and/or execution of plans and specifications required.

9.6 TERMINATION - ADVANCE PAYMENTS. Upon termination of this Lease pursuant to this paragraph 9, an equitable adjustment shall be made concerning advance rent and any advance payments made by Lessee to Lessor. Lessor shall, in addition, return to Lessee so much of Lessee's security deposit as has not ??? applied by Lessor.

#### 9.7 ?????

### 10. REAL PROPERTY TAXES.

10.1 PAYMENT OF TAXES. Lessor shall pay the real property tax, as defined in paragraph 10.3, applicable to the Office Building Project subject to reimbursement by Lessee of Lessee's Share of such taxes in accordance with the provisions of paragraph 4.2, except as otherwise provided in paragraph 10.2.

10.2 ADDITIONAL IMPROVEMENTS. Lessee shall not be responsible for paying any increase in real property tax specified in the tax assessor's records and work sheets as being caused by additional improvements placed upon the Office Building Project by other lessees or by Lessor for the exclusive enjoyment of any other lessee. Lessee shall, however, pay to Lessor at the time that Operating Expenses are payable under paragraph 4.2(c) the entirety of ??? increase in real property tax if assessed solely by reason of additional improvements placed upon the Premises by Lessee or at Lessee's request.

10.3 DEFINITION OF "REAL PROPERTY TAX". As used herein, the term "real property tax" shall include any form of real estate tax or assessment, general, special, ordinary or extraordinary, and any license fee, commercial rental tax, improvement bond or bonds, levy or tax (other than inheritance, personal income or estate taxes) imposed on the Office Building Project or any portion thereof by any authority having the direct or indirect power to tax, including any

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city, county, state or federal government, or any school, agricultural, sanitary, fire, street, drainage or other improvement district thereof, as against any legal or equitable interest of Lessor in the Office Building Project or in any portion thereof, as against Lessor's right to rent or other income therefrom, and as against Lessor's business of leasing the Office Building Project. The term "real property tax" shall also include any tax, fee, levy, assessment or charge (i) in substitution of, partially or totally, any tax, fee, levy, assessment or charge hereinabove included within the definition of "real property tax", or (ii) the nature which was heretofore included within the definition of "real property tax", or (iii) which is imposed for a service or right not charged prior to June 1, 1978 or if previously charged, has been increased since June 1, 1978, or (iv) which is imposed as a result of a change in ownership, as defined by applicable local statutes for property tax purposes, of the Office Building Project or which is added to a tax or charge hereinbefore included within the definition of real property tax by reason of such change of ownership, or (v) which is imposed by reason of this transaction, any modifications or changes hereto, or any transfers hereof.

10.4 JOINT ASSESSMENT. If the improvements or property, the taxes for which are to be paid separately by Lessee under paragraph 10.2 or 10.5 are separately assessed, Lessee's portion of that tax shall be equitably determined by Lessor from the respective valuations assigned in the assessor's work sheets or such other information (which may include the cost of construction) as may be reasonably available. Lessor's reasonable determination thereof, in good faith, shall be conclusive.

#### 10.5 PERSONAL PROPERTY TAXES.

(a) Lessee shall pay prior to delinquency all taxes assessed against and levied upon trade fixtures, furnishings, equipment and all other personal property of Lessee contained in the Premises or elsewhere.

(b) If any of Lessee's said personal property shall be assessed with Lessor's real property, Lessee shall pay to Lessor the taxes attributable to Lessee within ten (10) days after receipt of a written statement setting forth the taxes applicable to Lessee's property.

#### 11. UTILITIES.

11.1 SERVICES PROVIDED BY LESSOR. Lessor shall provide heating, ventilation, air conditioning, and janitorial service as reasonably required, reasonable amounts of electricity for normal lighting and office machines, water for reasonable and normal drinking and lavatory use, and replacement light bulbs and/or fluorescent tubes and ballasts for standard overhead fixtures.

11.2 SERVICES EXCLUSIVE TO LESSEE. Lessee shall pay for all water, gas, heat, light, power, telephone and other utilities and services specially or exclusively supplied and/or metered exclusively to the Premises or to Lessee, together with any taxes thereon. If any such services are not separately metered to the premises, Lessee shall pay at Lessor's option, either Lessee's Share or a reasonable proportion to be determined by Lessor of all charges jointly metered with other premises in the Building.

11.3 HOURS OF SERVICE. Said services and utilities shall be provided during generally accepted business days and hours or such other days or hours as may hereafter be set forth. Utilities and services required at other times shall be subject to advance request and reimbursement by Lessee to Lessor of the cost thereof.

11.4 EXCESS USAGE BY LESSEE. Lessee shall not make connection to the utilities except by or through existing outlets and shall not install or use machinery or equipment in or about the Premises that uses excess water, lighting or power, or suffer or permit any act that causes extra burden upon the utilities or services, including but not limited to security services, over standard office usage for the Office Building Project. Lessor shall require Lessee to reimburse Lessor for any excess expenses or costs that may arise out of a breach of this subparagraph by Lessee. Lessor may, in its sole discretion, install at Lessee's expense supplemental equipment and/or separate metering applicable to Lessee's excess usage or loading.

11.5 INTERRUPTIONS. There shall be no abatement of rent and Lessor shall not be liable in any respect whatsoever for the inadequacy, stoppage, interruption or discontinuance of any utility or service due to riot, strike, labor dispute, breakdown, accident, repair or other cause beyond Lessor's reasonable control or in cooperation with governmental request or directions.

## 12. ASSIGNMENT AND SUBLETTING.

12.1 LESSOR'S CONSENT REQUIRED. Lessee shall not voluntarily or by operation of law assign, transfer, mortgage, sublet, or otherwise transfer or encumber all or any part of Lessee's interest in the Lease or in the Premises, without Lessor's prior written consent, which Lessor shall not unreasonably withhold. Lessor shall respond to Lessee's request for consent hereunder in a timely manner and any attempted assignment, transfer, mortgage, encumbrance or subletting without such consent shall be void, and shall constitute a material default and breach of this Lease without the need for notice to Lessee under paragraph 13.1. "Transfer" within the meaning of this paragraph 12 shall include the transfer or transfers aggregating: (a) if Lessee is a corporation, more than twenty-five percent (25%) of the voting stock of such corporation, or (b) if Lessee is a partnership, more than twenty-five percent (25%) of the profit and loss participation in such partnership.

12.2 LESSEE AFFILIATE. Notwithstanding the provisions of paragraph 12.1 hereof, Lessee may assign or sublet the Premises, or any portion thereof, without Lessor's consent, to any corporation which controls, is controlled by or is under common control with Lessee, or to any corporation resulting from the merger or consolidation with Lessee, or to any person or entity which acquires all the assets of Lessee as a going concern of the business that is being conducted on the Premises, all of which are referred to as "Lessee Affiliate"; provided that before such assignment shall be effective, (a) said assignee shall assume, in full, the obligations of Lessee under this Lease and (b) Lessor shall be given written notice of such assignment and assumption. Any such assignment shall not, in any way, affect or limit the liability of Lessee under the terms of this Lease even if after such assignment or subletting the terms of this Lease are materially changed or altered without the consent of Lessee, the consent of whom shall not be necessary.

## 12.3 TERMS AND CONDITIONS APPLICABLE TO ASSIGNMENT AND SUBLETTING.

(a) Regardless of Lessor's consent, no assignment or subletting shall release Lessee of Lessee's obligation hereunder or alter the primary liability of Lessee to pay the rent and other sums due Lessor hereunder including Lessee's Share of Operating Expense Increase, and to perform all other obligations to be performed by Lessee hereunder.

(b) Lessor may accept rent from any person other than Lessee pending approval or disapproval of such assignment.

(c) Neither a delay in the approval or disapproval of such assignment or subletting, nor the acceptance of rent, shall constitute a waiver or estoppel of Lessor's right to exercise its remedies for the breach of any of

the terms or conditions of this paragraph 12 or this Lease.

(d) Lessee's obligation under this Lease have been guaranteed by third parties, then an assignment or sublease, and Lessor's consent thereto, shall not be effective unless said guarantors give their written consent to such sublease and the terms thereof.

(e) The consent by Lessor to any assignment or subletting shall not constitute a consent to any subsequent assignment or subletting by Lessee or to any subsequent or successive assignment or subletting by the sublessee. However, Lessor may consent to subsequent sublettings and assignments of the sublease or any amendments or modifications thereto without notifying Lessee or anyone else liable on the Lease or sublease and without obtaining their consent and such action shall not relieve such persons from liability under this Lease or said sublease; however, such persons shall not be responsible to the extent any such amendment or modification enlarges or increases the obligations of the Lessee or sublessee under this Lease or such sublease.

(f) In the event of any default under this Lease, Lessor may proceed directly against Lessee, any guarantors or anyone else responsible for the performance of this Lease, including the sublessee, without first exhausting Lessor's remedies against any other person or entity responsible therefor to Lessor, or any

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(h) The discovery of the fact that any financial statement relied upon by Lessor in giving its consent to an assignment or subletting was materially false shall, at Lessor's election, render Lessor's said consent null and void.

#### 12.4 ADDITIONAL TERMS AND CONDITIONS APPLICABLE TO SUBLETTING.

Regardless of Lessor's consent, the following terms and conditions shall apply to any subletting by Lessee of all or any part of the Premises and shall be deemed included in all subleases under this Lease whether or not expressly incorporated therein:

(a) Lessee hereby assigns and transfers to Lessor all of Lessee's interest in all rentals and income arising from any sublease heretofore or hereafter made by Lessee, and Lessor may collect such rent and income and apply same toward Lessee's obligations under this Lease; provided, however, ??? until a default shall occur in the performance of Lessee's obligations under this Lease, Lessee may receive, collect and enjoy the rents accruing under such sublease. Lessor shall not, by reason of this or any other assignment of such sublease to Lessor nor by reason of the collection of the rents from a sublessee, be deemed liable to the sublessee for any failure of Lessee to perform and comply with any of Lessee's obligations to such sublessee under such sublease. Lessee hereby irrevocably authorizes and directs any such sublessee, upon receipt of a written notice from Lessor stating that a default exists in

the performance of Lessee's obligations under this Lease, to pay to Lessor the rents due and to become due under the sublease. Lessee agrees that such sublessee shall have the right to rely upon any such statement and request from Lessor, and that such sublessee shall pay such rents to Lessor without an obligation or right to inquire as to whether such default exists and notwithstanding any notice from or claim from Lessee to the contrary Lessee shall have no right or claim against said sublessee or Lessor for any such rents so paid by said sublessee to Lessor.

(b) No sublease entered into by Lessee shall be effective unless and until it has been approved in writing by Lessor. In entering into any sublease, Lessee shall use only such form of sublease as is satisfactory to Lessor, and once approved by Lessor, such sublease shall not be changed or modified without Lessor's prior written consent. Any sublease shall, by reason of entering into a sublease under this Lease, be deemed for the benefit of Lessor, to have assumed and agreed to conform and comply with each and every obligation herein to be performed by Lessee other than such obligations as are contrary to or inconsistent with provisions contained in a sublease to which Lessor has expressly consented in writing.

(c) In the event Lessee shall default in the performance of its obligations under this Lease, Lessor at its option and without any obligation to do may require any sublessee to attorn to Lessor, in which event Lessor shall undertake the obligations of Lessee under such sublease from the time of the exercise of said option to the termination of such sublease; provided, however, Lessor shall not be liable for any prepaid rents or security deposit paid by such sublessee to Lessee or for any other prior defaults of Lessee under such sublease.

(d) No sublessee shall further assign or sublet all or any part of the Premises without Lessor's prior written consent.

(e) With respect to any subletting to which Lessor has consented, Lessor agrees to deliver a copy of any notice of default by Lessee to the sublessee. Such sublessee shall have the right to cure a default of Lessee within three (3) days after service of said notice of default upon such sublessee, and the sublessee shall have a right of reimbursement and offset from and against Lessee for any such defaults cured by the sublessee.

12.5 LESSOR'S EXPENSES. In the event Lessee shall assign or sublet the Premises or request the consent of Lessor to any assignment or subletting or if Lessee shall request the consent of Lessor for any act Lessee proposes to do then Lessee shall pay Lessor's reasonable costs and expenses incurred in connection therewith, including attorneys', architects', engineers' or other consultants' fees.

12.6 CONDITIONS TO CONSENT. Lessor reserves the right to condition any approval to assign or sublet upon Lessor's determination that (a) the proposed assignee or sublessee shall conduct a business on the Premises of a quality substantially equal to that of Lessee and consistent with the general character of the other occupants of the Office Building Project and not in violation of any exclusives or rights then held by other tenants, and (b) the proposed assignee or sublessee be at least as financially responsible as Lessee was expected to be at the time of the execution of this Lease or of such assignment or subletting, whichever is greater. See addendum paragraphs 54 and 55.

### 13. DEFAULT; REMEDIES.

13.1 Default. The occurrence of any one or more of the following events shall constitute a material default of this Lease by Lessee:

(a) The vacation or abandonment of the Premises by Lessee. Vacation of the Premises shall include the failure to occupy the Premises for a continuous period of sixty (60) days or more, whether or not the rent is paid.

(b) The breach by Lessee of any of the covenants, conditions or provisions of paragraphs 7.3(a), (b) or (d) (alterations), 12.1 (assignment or subletting), 13.1(a) (vacation or abandonment), 13.1(e) (insolvency), 13.1(f) (false statement), 16(a) (estoppel certificate), 30(b) (subordination), 33 (auctions), or 411 (easements), all of which are hereby deemed to be material, non-curable defaults without the necessity of any notice by Lessor to Lessee thereof.

(c) The failure by Lessee to make any payment of rent or any other payment required to be made by Lessee hereunder, as and when due, where such failure shall continue for a period of three (3) days after written notice

thereof from Lessor to Lessee. In the event that Lessor serves Lessee with a notice to Pay Rent or Quit pursuant to applicable Unlawful Detainer statutes such Notice to Pay Rent or Quit shall also constitute the notice required by this subparagraph.

(d) The failure by Lessee to observe or perform any of the covenants, conditions or provisions of this Lease to be observed or performed by Lessee, other than those referenced in subparagraphs (b) and (c), above, where such failure shall continue for a period of thirty (30) days after written notice thereof from Lessor to Lessee; provided, however, that if the nature of Lessee's noncompliance is such that more than thirty (30) days are reasonably required for its cure, then Lessee shall not be deemed to be in default if Lessee commenced such cure within said thirty (30) day period and thereafter diligently pursues such cure to completion. To the extent permitted by law, such thirty (30) day notice shall constitute the sole and exclusive notice required to be given to Lessee under applicable Unlawful Detainer statutes.

(e) (i) The making by Lessee of any general arrangement or general assignment for the benefit of creditors; (ii) Lessee becoming a "debtor" as defined in 11 U.S.C. Section 101 or any successor statute thereto (unless, in the case of a petition filed against Lessee, the same is dismissed within sixty (60) days; (iii) the appointment of a trustee or receiver to take possession of substantially all of Lessee's assets located at the Premises or of Lessee's interest in this Lease where possession is not restored to Lessee within thirty (30) days; or (iv) the attachment, execution or other judicial seizure of substantially all of Lessee's assets located at the Premises or of Lessee's interest in this Lease, where such seizure is not discharged within thirty (30) days. In the event that any provision of this paragraph 13.1(e) is contrary to any applicable law, such provision shall be of no force or effect.

(f) The discovery by Lessor that any financial statement given to Lessor by Lessee, or its successor in interest or by any guarantor of Lessee's obligation hereunder, was materially false.

13.2 REMEDIES. In the event of any material default or breach of this Lease by Lessee, Lessor may at any time thereafter, with or without notice or demand and without limiting Lessor in the exercise of any right or remedy which Lessor may have by reason of such default:

(a) Terminate Lessee's right to possession of the Premises by any lawful means, in which case this Lease and the term hereof shall terminate and Lessee shall immediately surrender possession of the Premises to Lessor. In such event Lessor shall be entitled to recover from Lessee all damages incurred by Lessor by reason of Lessee's default including, but not limited to, the cost of recovering possession of the Premises; expenses of reletting, including necessary renovation and alteration of the Premises, reasonable attorneys' fees, and any real estate commission actually paid; the worth at the time ??? by the court having jurisdiction thereof of the amount by which the unpaid rent for the balance of the term after the time of such award exceeds the amount of such rental loss for the same period that Lessee proves could be reasonably avoided; that portion of the leasing commission paid by Lessor pursuant to paragraph 15 applicable to the unexpired term of this Lease.

(b) Maintain Lessee's right to possession in which case this Lease shall continue in effect whether or not Lessee shall have vacated or abandoned the Premises. In such event Lessor shall be entitled to enforce all of Lessor's rights and remedies under this Lease, including the right to recover the rent as it becomes due hereunder.

(c) Pursue any other remedy now or hereafter available to Lessor under the laws or judicial decisions of the state wherein the Premises are located. Unpaid installments of rent and other unpaid monetary obligations of Lessee under the terms of this Lease shall bear interest from the date due at the minimum rate then allowable by law.

13.3 DEFAULT BY LESSOR. Lessor shall not be in default unless Lessor fails to perform obligations required of Lessor within a reasonable time, but



in no event later than thirty (30) days after written notice by Lessee to Lessor and to the holder of any first mortgage or deed of trust covering the Premises whose name and address shall have theretofore been furnished to Lessee in writing, specifying wherein Lessor has failed to perform such obligation; provided, however, that if the nature of Lessor's obligation is such that more than thirty (30) days are required for performance then Lessor shall not be in default if Lessor commences performance within such 30-day period and thereafter diligently pursues the same to completion.

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ascertain. Such costs include, but are not limited to, processing and accounting charges, and late charges which may be imposed on Lessor by the terms of any mortgage or trust deed covering the Office Building Project. Accordingly, if any installment of Base Rent, Operating Expense Increase, or any other sum due from Lessee shall not be received by Lessor or Lessor's designee within ten (10) days after such amount shall be due, then, without any requirement for notice for Lessee, Lessee shall pay to Lessor a late charge equal to 6% of such overdue amount. The parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Lessor will incur by reason of late payment by Lessee. Acceptance of such late charge by Lessor shall in no event constitute a waiver of Lessee's default with respect to such overdue amount, nor prevent Lessor from exercising any of the other rights and remedies granted hereunder.

Condemnation. If the Premises or any portion thereof or the Office Building Project are taken under the power of eminent domain, or sold under the threat at the exercise of said power (all of which are herein called "condemnation"), this Lease shall terminate as to the part so taken as of the date the condemning authority takes title or possession, whichever first occurs; provided that is so much of the Premises or the Office Building Project are taken by such condemnation as would substantially and adversely affect the operation and profitability of Lessee's business conducted from Premises, Lessee

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shall have the option, to be exercised only in writing within thirty (30) days after Lessor shall have given Lessee written notice of such taking (or in the absence of such notice, within thirty (30) days after the condemning authority shall have taken possession), to terminate this Lease as of the date the condemning authority takes such possession. If Lessee does not terminate this Lease in accordance with the foregoing, this Lease shall remain in full force and effect as to the portion of the Premises remaining, except that the rent and Lessee's Share of Operating Expense Increase shall be reduced in the proportion that the floor area of the Premises taken bears to the total floor area of the Premises. Common Areas taken shall be excluded from the Common Areas usable by Lessee and no reduction of rent shall occur with respect thereto or by reason thereof. Lessor shall have the option in its sole discretion to terminate this Lease as of the taking of possession by the condemning authority, by giving written notice to Lessee of such election within thirty (30) days after receipts of notice of a taking by condemnation of any part of the Premises or the Office Building Project. Any award for the taking of all or any part of the Premises or the Office Building Project under the power of eminent domain or any payment made under threat of the exercise of such power shall be the property of Lessor, whether such award shall be made as compensation for diminution in value of the leasehold or for the taking of the fee, or as severance damages; provided, however, that Lessee shall be entitled to any separate award for loss of or damage to Lessee's trade fixtures,

removable personal property and unamortized tenant improvements that have been paid for by Lessee. For that purpose the cost of such improvements shall be amortized over the original term of this Lease excluding any options. In the event that this Lease is not terminated by reason of such condemnation, Lessor shall to the extent of severance damages received by Lessor in connection with such condemnation, repair any damage to the Premises caused by such condemnation except to the extent that Lessee has been reimbursed therefor by the condemning authority. Lessee shall pay any amount in excess of such severance damages required to complete such repair.

15. BROKER'S FEE.

(a) The brokers involved in this transaction are Leonard & Ohren as "listing broker" and Grubb & Ellis/Beach Real Estate as "cooperating broker," licensed real estate broker(s). A "cooperating broker" is defined as any broker other than the listing broker entitled to a share of any commission arising under this Lease. Upon execution of this Lease by both parties, Lessor shall pay to said brokers jointly, or in such separate shares as they may mutually designate in writing, a fee as set forth in a separate agreement between Lessor and said broker(s), or in the event there is no separate agreement between Lessor and said broker(s), the sum of \$\_\_\_\_\_ per separate agreement, for brokerage services rendered by said broker(s) to Lessor in this transaction.

(b) Lessor agrees to pay said fee not only on behalf of Lessor but also on behalf of any person, corporation, association, or other entity having an ownership interest in said real property or any part thereof, when such fee is due hereunder. Any transferee of Lessor's interest in this Lease, whether such transfer is by agreement or by operation of law, shall be deemed to have assumed Lessor's obligation under this paragraph 15. Each listing and cooperating broker shall be a third party beneficiary of the provisions of this paragraph 15 to the extent of their interest in any commission arising under this Lease and may enforce that right directly against Lessor, provided, however, that all brokers having a right to any part of such total commission shall be a necessary party to any suit with respect thereto.

(c) Lessee and Lessor each represent and warrant to the other that neither has had any dealings with any person, firm, broker or finder (other than the person(s), if any, whose names are set forth in paragraph 15(a), above) in connection with the negotiation of this Lease and/or the consummation of the transaction contemplated hereby, and no other broker or other person, firm or entity is entitled to any commission or finder's fee in connection with said transaction and Lessee and Lessor do each hereby indemnify and hold the other harmless from and against any costs, expenses, attorneys' fees or liability for compensation or charges which may be claimed by any such unnamed broker, finder or other similar party by reason of any dealings or actions of the indemnifying party.

16. ESTOPPEL CERTIFICATE.

(a) Each party (as "responding party") shall at any time upon not less than ten (10) days' prior written notice from the other party ("requesting party") execute, acknowledge and deliver to the requesting party a statement in writing (i) certifying that this Lease is unmodified and in full force and effect (or, if modified, stating the nature of such modification and certifying that this Lease, as so modified, is in full force and effect) and the date to which the rent and other charges are paid in advance, if any, and (ii) acknowledging that there are not, to the responding party's knowledge, any uncured defaults on the part of the requesting party, or specifying such defaults if any are claimed. Any such statement may be conclusively relied upon by any prospective purchaser or encumbrancer of the Office Building Project or of the business of Lessee.

(b) At the requesting party's option, the failure to deliver such statement within such time shall be a material default of this Lease by the party who is to respond, without any further notice to such party, or it shall be conclusive upon such party that (i) this Lease is in full force and effect, without modification except as may be represented by the requesting party, (ii) there are no incurred defaults in the requesting party's performance, and (iii)

if Lessor is the requesting party, not more than one month's rent has been paid in advance.

(c) If Lessor desires to finance, refinance, or sell the Office Building Project, or any part thereof, Lessee hereby agrees to deliver to any lender or purchaser designated by Lessor such financial statements of Lessee as may be reasonably required by such lender or purchaser. Such statements shall include the past three (3) years' financial statements of Lessee. All such financial statements shall be received by Lessor and such lender or purchaser in confidence and shall be used only for the purposes herein set forth.

17. LESSOR'S LIABILITY. The term "Lessor" as used herein shall mean only the owner or owners, at the time in question, of the fee title or a lessee's interest in a ground lease of the Office Building Project, and except as expressly provided in paragraph 15, in the event of any transfer of such title or interest, Lessor herein named (and in case of any subsequent transfers then the grantor) shall be relieved from and after the date of such transfer of all liability as respects Lessor's obligations thereafter to be performed, provided that any funds in the hands of Lessor or the then grantor at the time of such transfer, in which Lessee has an interest, shall be delivered to the grantee. The obligations contained in this Lease to be performed by Lessor shall, subject as aforesaid, be binding on Lessor's successors and assigns, only during their respective periods of ownership.

18. SEVERABILITY. The invalidity of any provision of this Lease as determined by a court of competent jurisdiction shall in no way affect the validity of any other provision hereof.

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Except as expressly herein provided, any amount due to Lessor not paid when due shall bear interest at maximum rate then allowable by law or judgments from the date due. Payment of such interest shall not excuse or cure any default by Lessee under this Lease; provided, however, that interest shall not be payable on late charges incurred by Lessee nor on any amounts upon which late charges are paid by Lessee.

20. TIME OF ESSENCE. Time is of the essence with respect to the obligations to be performed under this Lease.

21. ADDITIONAL RENT. All monetary obligations of Lessee to Lessor under the terms of this Lease, including but not limited to Lessee's Share of Operating Expense Increase and any other expenses payable by Lessee hereunder shall be deemed to be rent.

22. INCORPORATION OF PRIOR AGREEMENTS; AMENDMENTS. This Lease contains all agreements of the parties with respect to any matter mention herein. No prior or contemporaneous agreement or understanding pertaining to any such matter shall be effective. This Lease may be modified in writing only, signed by

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the parties in interest at the time of the modification. Except as otherwise stated in this Lease, Lessee hereby acknowledges that neither the real estate broker listed in paragraph 15 hereof nor any cooperating broker on this transaction nor the Lessor or any employee or agents of any said persons has made any oral or written warranties or representations to Lessee relative to the condition or use by Lessee of the Premises or the Office Building Project and Lessee acknowledges that Lessee assumes all responsibility regarding the Occupational Safety Health Act, the legal use and adaptability of the Premises and the compliance thereof with all applicable laws and regulations in effect during the term of this Lease.

23. NOTICES. Any notice required or permitted to be given hereunder shall be in writing and may be given by personal delivery or by certified or registered

mail, and shall be deemed sufficiently given if delivered or addressed to Lessee or to Lessor at the address noted below or adjacent to the signature of the respective parties, as the case may be. Mailed notices shall be deemed given upon actual receipt at the address required, or forty-eight hours following deposit in the mail, postage prepaid, whichever first occurs. Either party may by notice to the other specify a different address for notice purposes except that ?? Lessee's taking possession of the Premises, the Premises shall constitute Lessee's address for notice purposes. A copy of all notices required or permitted to be given to Lessor hereunder shall be concurrently transmitted to such party or parties at such addresses as Lessor may from time to time hereafter designate by notice to Lessee.

24. WAIVERS. No waiver by Lessor of any provision hereof shall be deemed a waiver of any other provision hereof or of any subsequent breach by Lessee of the same or any other provision. Lessor's consent to, or approval of, any act shall not be deemed to render unnecessary the obtaining of Lessor's consent to or approval of any subsequent act by Lessee. The acceptance of rent hereunder by Lessor shall not be a waiver of any preceding breach by Lessee of any provision hereof, other than the failure of Lessee to pay the particular rent so accepted, regardless of Lessor's knowledge of such preceding breach at the time of acceptance of such rent.

25. RECORDING. Either Lessor or Lessee shall, upon request of the other, execute, acknowledge and deliver to the other a "short form" memorandum of this Lease for recording purposes.

26. HOLDING OVER. If Lessee, with Lessor's consent, remains in possession of the Premises or any part thereof after the expiration of the term hereof, such occupancy shall be a tenancy from month to month upon all the provisions of this Lease pertaining to the obligations of Lessee, except that the rent payable shall be two hundred percent (200%) of the rent payable immediately preceding the termination date of this Lease, and all Options, if any, granted under the terms of this Lease shall be deemed terminated and be of no further effect during said month to month tenancy.

27. CUMULATIVE REMEDIES. No remedy or election hereunder shall be deemed exclusive but shall, wherever possible, be cumulative with all other remedies at law or in equity.

28. COVENANTS AND CONDITIONS. Each provision of this Lease performable by Lessee shall be deemed both a covenant and a condition.

29. BINDING EFFECT; CHOICE OF LAW. Subject to any provision hereof restricting assignment or subletting by Lessee and subject to the provision of paragraph 17, this Lease shall bind the parties, their personal representatives, successors and assign. This Lease shall be governed by the laws of the State where the Office Building Project is located and any litigation concerning this Lease between the parties hereto shall be initiated in the county in which the Office Building Project is located.

30. SUBORDINATION.

(a) This Lease, and any Option or right of first refusal granted hereby, at Lessor's option, shall be subordinate to any ground lease, mortgage, deed of trust, or any other hypothecation or security now or hereafter placed upon the Office Building Project and to any and all advances made on the security thereof and to all renewals, modifications, consolidations, replacements and extensions thereof. Notwithstanding such subordination, Lessee's right to quiet possession of the Premises shall not be disturbed if Lessee is not in default and so long as Lessee shall pay the rent and observe and perform all of the provisions of this Lease, unless this Lease is otherwise terminated pursuant to its terms. If any mortgagee, trustee or ground lessor shall elect to have this Lease and any Options granted hereby prior to the lien of its mortgage, deed of trust or ground lease, and shall give written notice thereof to Lessee, this Lease and such Option shall be deemed prior to such mortgage, deed of trust or ground lease, whether this Lease or such Options are dated prior or subsequent to the date of said mortgage, deed of trust or ground lease or the date of recording thereof.

(b) Lessee agrees to execute any documents required to effectuate an attornment, a subordination, or to make this Lease or any Option granted herein prior to the lien of any mortgage, deed of trust or ground lease, as the case may be. Lessee's failure to execute such documents within ten (10) days after written demand shall constitute a material default by Lessee hereunder without further notice to Lessee or, at Lessor's option, Lessor shall execute such documents on behalf of Lessee as Lessee's attorney-in-fact. Lessee does hereby make, constitute and irrevocably appoint Lessor as Lessee's attorney-in-fact and in Lessee's name, place and stead, to execute such documents in accordance with this paragraph 30(b).

31. ATTORNEY'S FEES.

31.1 If either party or the broker(s) named herein bring an action to enforce the terms hereof or declare rights hereunder, the prevailing party in any such action, trial, or appeal thereon, shall be entitled to his reasonable attorneys' fees to be paid by the losing party as fixed by the court in the same or separate suit, and whether or not such action is pursued to decision or judgment. The provisions of this paragraph shall inure to the benefit of the broker named herein who seeks to enforce a right hereunder.

31.2 The attorneys' fee award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all attorneys' fees reasonably incurred in good faith.

31.3 Lessor shall be entitled to reasonable attorneys' fees and all other costs and expenses incurred in the preparation and service of notices of default and consultations in connection therewith, whether or not a legal transaction is subsequently commenced in connection with such default.

32. LESSOR'S ACCESS.

32.1 Lessor and Lessor's agents shall have the right to enter the Premises at reasonable times for the purpose of inspecting the same, performing any service required of Lessor, showing the same to prospective purchasers, lenders, or lessees, taking such safety measures, erecting such scaffolding or other necessary structures, making such alterations, repairs, improvements or additions to the Premises or to the Office Building Project as Lessor may reasonably deem necessary or desirable and the erecting, using and maintaining of utilities, services, pipes and conduits through the Premises and/or other premises as long as there is no material adverse effect to Lessee's use of the Premises. Lessor may at any time place on or about the Premises or the Building any ordinary "For Sale" signs and Lessor may at any time during the last 120 days of the term hereof place on or about the Premises any ordinary "For Lease" signs. [Illegible]

32.3 Lessor shall [Illegible] in the case of emergency to enter the Premises by any reasonably appropriate means, and any such entry shall not be deemed a forceable or unlawful entry or detainer of the Premises or an eviction. Lessee waives any charges for damages or injuries or interference with Lessee's property or business in connection therewith.

33. AUCTIONS. Lessee shall not conduct, nor permit to be conducted, either voluntarily or involuntarily, any auction upon the Premises or the Common Areas without first having obtained Lessor's prior written consent. Notwithstanding anything to the contrary in this Lease, Lessor shall not be obligated to exercise any standard of reasonableness in determining whether to grant such consent. The holding of any auction on the Premises or Common Areas in violation of this paragraph shall constitute a material default of this Lease.

34. SIGNS. Lessee shall not place any sign upon the Premises or the Office Building Project without Lessor's prior written consent. Under no circumstances shall Lessee place a sign on any roof of the Office Building Project.

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and shall, at the option of Lessor, terminate all or any existing subtenancies or may, at the option of Lessor, operate as an assignment to Lessor or any or all of such subtenancies.

36. CONSENTS. Except for paragraphs 33 (auctions) and 34 (signs) hereof, wherever in this Lease the consent of one party is required to an act of the other party such consent shall not be unreasonably withheld or delayed.

37. GUARANTOR. In the event that there is a guarantor of this Lease, said guarantor shall have the same obligations as Lessee under this Lease.

38. QUIET POSSESSION. Upon Lessee paying the rent for the Premises and observing and performing all of the covenants, conditions and provisions on Lessee's part to be observed and performed hereunder, Lessee shall have quiet possession of the Premises for the entire term hereof subject to all of the provisions of this Lease. The individuals executing this Lease on behalf of Lessor represent and warrant to Lessee that they are fully authorized and legally capable of executing this Lease on behalf of Lessor and that such execution is binding upon all parties holding an ownership interest in the Office Building Project.

39. OPTIONS.

39.1 DEFINITION. As used in this paragraph the word "Option" has the following meaning: (1) the right or option to extend the term of this Lease or to renew this Lease or to extend or renew any lease that Lessee has on other property of Lessor; (2) the option of right of first refusal to lease the Premises or the right of first offer to lease the Premises or the right of first refusal to lease other space within the Office Building Project or other property of Lessor or the right of first offer to lease other space within the Office Building Project or other property of Lessor; (3) the right or option to purchase the Premises or the Office Building Project, or the right of first refusal to purchase the Premises or the Office Building Project or the right of first offer to purchase the Premises or the Office Building Project, or the right or option to purchase other property of Lessor, or the right of first refusal to purchase other property of Lessor or the right of first offer to purchase other property of Lessor.

39.2 OPTIONS PERSONAL. Each Option granted to Lessee in this Lease is personal to the original Lessee and may be exercised only by the original Lessee while occupying the Premises who does so without the intent of thereafter assigning this Lease or subletting the Premises or any portion thereof, and may not be exercised or be assigned, voluntarily or involuntarily, by or to any person or entity other than Lessee; provided, however, that an Option may be exercised by or assigned to any Lessee Affiliate as defined in paragraph 12.2 of this Lease. The Options, if any, herein granted to Lessee are not assignable separate and apart from this Lease, nor may any Option be separated from this Lease in any manner, either by reservation or otherwise.

39.3 MULTIPLE OPTIONS. In the event that Lessee has any multiple options to extend or renew this Lease a later option cannot be exercised unless the prior option to extend or renew this Lease has been so exercised.

39.4 EFFECT OF DEFAULT ON OPTIONS.

(a) Lessee shall have no right to exercise an Option, notwithstanding any provision in the grant of Option to the contrary, (i) during the time commencing from the date Lessor gives to Lessee a notice of default pursuant to paragraph 13.1(c) or 13.3(d) and continuing until the noncompliance alleged in said notice of default is cured, or (ii) during the period of time commencing on the day after a monetary obligation to Lessor is due from Lessee and unpaid (without any necessity for notice thereof to Lessee) and continuing until the obligation is paid, or (iii) in the event that Lessor has given to Lessee three

or more notices of default under paragraph 13.1(c), or paragraph 13.1(d), whether or not the defaults are cured, during the 12 month period of time immediately prior to the time that Lessee attempts to exercise the subject Option, (iv) if Lessee has committed any non-curable breach, including without limitation those described in paragraph 13.1(b), or is otherwise in default of any of the terms, covenants or conditions of this Lease.

(b) The period of time within which an Option may be exercised shall not be extended or enlarged by reason of Lessee's inability to exercise an Option because of the provisions of paragraph 39.4(a).

(c) All rights of Lessee under the provisions of an Option shall terminate and be of no further force or effect, notwithstanding Lessee's due and timely exercise of the Option, if, after such exercise and during the term of this Lease, (i) Lessee fails to pay to Lessor a monetary obligation of Lessee for a period of thirty (30) days after such obligation becomes due (without any necessity of Lessor to give notice thereof to Lessee), or (ii) Lessee fails to commence to cure a default specified in paragraph 13.1(d) within thirty (30) days after the date that Lessor gives notice to Lessee of such default and/or Lessee fails thereafter to diligently prosecute said cure to completion, or (iii) Lessor gives to Lessee three or more notices of default under paragraph 13.1(c), or paragraph 13.1(d), whether or not the defaults are cured, or (iv) if Lessee has committed any non-curable breach, including without limitation those described in paragraph 13.1(b), or is otherwise in default of any of the terms, covenants and conditions of this Lease.

#### 40. SECURITY MEASURES - LESSOR'S RESERVATIONS.

40.1 Lessee hereby acknowledges that Lessor shall have no obligation whatsoever to provide guard service or other security measures for the benefit of the Premises or the Office Building Project. Lessee assumes all responsibility for the protection of Lessee, its agents, and invitees and the property of Lessee and of Lessee's agents and invitees from acts of third parties. Nothing herein contained shall prevent Lessor, at Lessor's sole option, from providing security protection for the Office Building Project or any part thereof, in which event the cost thereof shall be included within the definition of Operating Expenses, as set forth in paragraph 4.2(b).

40.2 Lessor shall have the following rights:

(a) To change the name, address or title of the Office Building Project or building in which the Premises are located upon not less than 90 days prior written notice;

(b) To, at Lessee's expense, provide and install Building standard graphics on the door of the Premises and such portions of the Common Areas as Lessor shall reasonably deem appropriate;

(c) To permit any lessee the exclusive right to conduct any business as long as such exclusive does not conflict with any rights expressly given herein;

(d) To place such signs, notices or displays as Lessor reasonably deems necessary or advisable upon the roof, exterior of the buildings or the Office Building Project or on pole signs in the Common Areas;

40.3 Lessee shall not:

(a) Use a representation (photographic or otherwise) of the Building or the Office Building Project or their name(s) in connection with Lessee's business;

(b) Suffer or permit anyone, except in emergency, to go upon the roof of the Building.

#### 41. EASEMENTS.

41.1 Lessor reserves to itself the right, from time to time, to grant such

easements, rights and dedications that Lessor deems necessary or desirable, and to cause the recordation of Parcel Maps and restrictions, so long as such easements, rights, dedications, Maps and restrictions do not unreasonably interfere with the use of the Property by Lessee. Lessee shall sign any of the aforementioned documents upon request of Lessor and failure to do so shall ?? [ILLEGIBLE COPY] way affect this Lease or impose any liability upon Lessor.

42. PERFORMANCE UNDER PROTEST. If at any time a dispute shall arise as to any amount or sum to be paid by one party to the other under the provisions hereof, the party against whom the obligation to pay the money is asserted shall have the right to make payment "under protest" and such payment shall not be regarded as a voluntary payment, and there shall survive the right on the part of said party to institute suit for recovery of such sum. If it shall be adjudged that there was no legal obligation on the part of said party to pay such sum or any part thereof, said party shall be entitled to recover such sum or so much thereof as it was not legally required to pay under the provisions of this Lease.

43. AUTHORITY. If Lessee is a corporation, trust, or general or limited partnership, Lessee, and such individual executing this Lease on behalf of such entity represent and warrant that such individual is duly authorized to execute and deliver this Lease on behalf of said entity. If Lessee is a corporation, trust or partnership, Lessee shall, without thirty (30) days after execution of this Lease, deliver to Lessor evidence of such authority satisfactory to Lessor.

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44. CONFLICT. Any conflict between the printed provisions, Exhibits or Addenda of this Lease and the typewritten or handwritten provisions, if any, shall be controlled by the typewritten or handwritten provisions.

45. NO OFFER. Preparation of this Lease by Lessor or Lessor's agent and submission of same to Lessee shall not be deemed an offer to Lessee to lease. This Lease shall become binding upon Lessor and Lessee only when fully executed by both parties.

46. LENDER MODIFICATION. Lessee agrees to make such reasonable modifications to this Lease as may be reasonably required by an institutional lender in connection with the obtaining of normal financing or refinancing of the Office Building Project.

47. MULTIPLE PARTIES. If more than one person or entity is named as either Lessor or Lessee herein, except as otherwise expressly provided herein, the obligations of the Lessor or Lessee herein shall be the joint and several responsibility of all persons or entities named herein as such Lessor or Lessee, respectively.

48. WORK LETTER. This Lease is supplemented by that certain Work Letter of even date executed by Lessor and Lessee, attached hereto as Exhibit C, and incorporated herein by this reference.

49. ATTACHMENTS. Attached hereto are the following documents which constitute a part of this Lease:

LESSOR AND LESSEE HAVE CAREFULLY READ AND REVIEWED THIS LEASE AND EACH TERM AND PROVISION CONTAINED HEREIN AND, BY EXECUTION OF THIS LEASE, SHOW THEIR INFORMED AND VOLUNTARY CONSENT THERETO. THE PARTIES HEREBY AGREE THAT, AT THE TIME THIS LEASE IS EXECUTED, THE TERMS OF THIS LEASE ARE COMMERCIALY REASONABLE AND EFFECTUATE THE INTENT AND PURPOSE OF LESSOR AND LESSEE WITH RESPECT TO THE PREMISES.



IF THIS LEASE HAS BEEN FILLED IN IT HAS BEEN PREPARED FOR SUBMISSION TO YOUR ATTORNEY FOR HIS APPROVAL. NO REPRESENTATION OR RECOMMENDATION IS MADE BY THE AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION OR BY THE REAL ESTATE BROKER OR ITS AGENTS OR EMPLOYEES AS TO THE LEGAL SUFFICIENCY, LEGAL EFFECT, OR TAX CONSEQUENCES OF THIS LEASE OR THE TRANSACTION RELATING THERETO; THE PARTIES SHALL RELY SOLELY UPON THE ADVICE OF THEIR OWN LEGAL COUNSEL AS TO THE LEGAL AND TAX CONSEQUENCES OF THIS LEASE.

LESSOR

LESSEE

Pacifica California/Apollo, Inc.

Skechers USA, Inc.

By /s/ STEVEN OHREN

By /s/ DAVID WEINBERG

Its Manager, Steven Ohren

Its CFO, David Weinberg

By

By /s/ PHILIP G. PACCIONE

Its

Its General Counsel, Philip G. Paccione

Executed at 330 Washington Blvd., Suite 300

Executed at

on

on

Address 330 Washington Blvd.

Address

NOTE: These forms are often modified to meet changing requirements of law and needs of the industry. Always write or call to make sure you are utilizing the most current form: AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION, 700 South Flower Street, Suite 600, Los Angeles, CA 90017, (213) 687-8777.

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STANDARD OFFICE LEASE  
FLOOR PLAN

[DIAGRAM OF FLOOR PLAN]

EXHIBIT A

13

RULES AND REGULATIONS FOR  
STANDARD OFFICE LEASE

[A.I.R. LOGO]

Dated: November 18, 1999

By and Between Pacific California/Apollo, LLC and Skechers USA, Inc.

GENERAL RULES

1. Lessee shall not suffer or permit the obstruction of any Common Areas, including driveways, walkways and stairways.
2. Lessor reserves the right to refuse access to any persons Lessor in good faith judges to be a threat to the safety and reputation of the Office Building Project and its occupants.
3. Lessee shall not make or permit any noise or odors that annoy or interfere with other lessees or persons having business within the Office Building Project.
4. Lessee shall not keep animals or birds within the Office Building Project, and shall not bring bicycles, motorcycles or other vehicles into areas not designated as authorized for same.
5. Lessee shall not make, suffer or permit litter except in appropriate receptacles for that purpose.
6. Lessee shall not alter any lock or install new or additional locks or bolts.
7. Lessee shall be responsible for the inappropriate use of any toilet rooms, plumbing or other utilities. No foreign substances of any kind are to be inserted therein.
8. Lessee shall not deface the walls, partitions or other surfaces of the Office Building Project.
9. Lessee shall not suffer or permit anything in or around the Premises or Building that causes excessive vibration or floor loading in any part of the Office Building Project.
10. Furniture, significant freight and equipment shall be moved into or out of the building only with the Lessor's knowledge and consent, and subject to such reasonable limitations, techniques and timing, as may be designated by Lessor. Lessee shall be responsible for any damage to the Office Building Project arising from any such activity.
11. Lessee shall not employ any service or contractor for services or work to be performed in the Building, except as approved by Lessor.
12. Lessor reserves the right to close and lock the Building on Saturdays, Sundays and legal holidays, and on other days between the hours of 7 P.M. and 7 A.M. of the following day. If Lessee uses the Premises during such periods, Lessee shall be responsible for securely locking any doors it may have opened for entry.
13. Lessee shall return all keys at the termination of its tenancy and shall be responsible for the cost of replacing any keys that are lost.
14. No window coverings, shades or awnings shall be installed or used by Lessee.
15. No Lessee, employee or invitee shall go upon the roof of the Building.
16. Lessee shall not suffer or permit smoking or carrying of lighted cigars or cigarettes in areas reasonably designated by Lessor or by applicable governmental agencies as non-smoking areas.
17. Lessee shall not use any method of heating or air conditioning other than as provided by Lessor.

18. Lessee shall not install, maintain or operate any vending machines upon the Premises without Lessor's written consent.

19. The Premises shall not be used for lodging or manufacturing, cooking or food preparation.

20. Lessee shall comply with all safety, fire protection and evacuation regulations established by Lessor or any applicable governmental agency.

21. Lessor reserves the right to waive any one of these rules or regulations, and/or as to any particular Lessee, and any such waiver shall not constitute a waiver of any other rule or regulation or any subsequent application thereof to such Lessee.

22. Lessee assumes all risks from theft or vandalism and agrees to keep its Premises locked as may be required.

23. Lessor reserves the right to make such other reasonable rules and regulations as it may from time to time deem necessary for the appropriate operation and safety of the Office Building Project and its occupants. Lessee agrees to abide by these and such rules and regulations.

#### PARKING RULES

1. Parking areas shall be used only for parking by vehicles no longer than full size, passenger automobiles herein called "Permitted Size Vehicles." Vehicles other than Permitted Size Vehicles are herein referred to as "Oversized Vehicles."

2. Lessee shall not permit or allow any vehicles that belong to or are controlled by Lessee or Lessee's employees, suppliers, shippers, customers, or invitees to be loaded, unloaded, or parked in areas other than those designated by Lessor for such activities.

3. Parking stickers or identification devices shall be the property of Lessor and be returned to Lessor by the holder thereof upon termination of the holder's parking privileges. Lessee will pay such replacement charge as is reasonably established by Lessor for the loss of such devices.

4. Lessor reserves the right to refuse the sale of monthly identification devices to any person or entity that willfully refuses to comply with the applicable rules, regulations, laws and/or agreements.

5. Lessor reserves the right to relocate all or a part of parking spaces from floor to floor, within one floor, and/or to reasonably adjacent offsite location(s), and to reasonably allocate them between compact and standard size spaces, as long as the same complies with applicable laws, ordinances and regulations.

6. Users of the parking area will obey all posted signs and park only in the areas designated for vehicle parking.

7. Unless otherwise instructed, every person using the parking area is required to park and lock his own vehicle. Lessor will not be responsible for any damage to vehicles, injury to persons or loss of property, all of which risks are assumed by the party using the parking area.

8. Validation, if established, will be permissible only by such method or methods as Lessor and/or its licensee may establish at rates generally applicable to visitor parking.

9. The maintenance, washing, waxing or cleaning of vehicles in the parking structure or Common Areas is prohibited.

10. Lessee shall be responsible for seeing that all of its employees, agents and invitees comply with the applicable parking rules, regulations, laws and agreements.

11. Lessor reserves the right to modify these rules and/or adopt such other reasonable and non-discriminatory rules and regulations as it may deem necessary for the proper operation of the parking area.

12. Such parking use as is herein provided is intended merely as a license only and no bailment is intended or shall be created hereby.

EXHIBIT B

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[A.I.R. LOGO]  
RENT ADJUSTMENT(S)  
STANDARD LEASE ADDENDUM

Dated November 17, 1999

By and Between (Lessor) Pacifica California/Apollo, LLC

(Lessee) Skechers USA, Inc.

Address of Premises: 225 S. Sepulveda Boulevard

Paragraph 50

A. RENT ADJUSTMENTS:

The monthly rent for each month of the adjustment period(s) specified below shall be increased using the method(s) indicated below:

(Check Method(s) to be Used and Fill in Appropriately)

I. Cost of Living Adjustment(s) (COLA)

a. On (Fill in COLA Dates): January 2, 2001, January 2, 2002, January 2, 2003, January 2, 2004 the Base Rent shall be adjusted by the change, if any, from the Base Month specified below, in the Consumer Price Index of the Bureau of Labor Statistics of the U.S. Department of Labor for (select one):  CPI W (Urban Wage Earners and Clerical Workers) or  CPI U (All Urban Consumers), for (Fill in Urban Area): Los Angeles/Long Beach, All Items (1982-1984 = 100), herein referred to as "CPI". A minimum increase of three percent (3%) and a maximum increase of five percent (5%) per annum shall be applied.

b. The monthly rent payable in accordance with paragraph A.I.a. of this Addendum shall be calculated as follows: the Base Rent set forth in paragraph 1.5 of the attached Lease, shall be multiplied by a fraction the numerator of which shall be the CPI of the calendar month two months prior to the month(s) specified in paragraph A.I.a. above during which the adjustment is to take effect, and the denominator of which shall be the CPI of the calendar month which is two months prior to (select one):  the first month of the term of this Lease as set forth in paragraph 1.3 ("Base Month") or  (Fill in Other "Base Month"): \_\_\_\_\_ . The sum so calculated shall constitute the new monthly rent hereunder, but in no event, shall any such new monthly rent be less than the rent payable for the month immediately preceding the rent adjustment.

c. In the event the compilation and/or publication of the CPI shall be transferred to any other governmental department or bureau or agency or shall be

discontinued, then the index most nearly the same as the CPI shall be used to make such calculation. In the event that the Parties cannot agree on such alternative index, then the matter shall be submitted for decision to the American Arbitration Association in accordance with the then rules of said Association and the decision of the arbitrators shall be binding upon the parties. The cost of said Arbitration shall be paid equally by the Parties.

RENT ADJUSTMENTS  
Page 1 of 2

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B. NOTICE:

Unless specified otherwise herein, notice of any such adjustments, other than Fixed Rental Adjustments, shall be made as specified in paragraph 23 of the Lease.

C. BROKER'S FEE:

The Brokers specified in paragraph 1.10 shall be paid a Brokerage Fee for each adjustment specified above in accordance with paragraph 15 of the Lease.

RENT ADJUSTMENTS  
Page 2 of 2

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[A.I.R. LOGO]

OPTION(S) TO EXTEND  
STANDARD LEASE ADDENDUM

Dated November 18, 1999

By and Between (Lessor) Pacifica California/Apollo, LLC

(Lessee) Skechers USA, Inc.

Address of Premises: 225 S. Sepulveda Boulevard, Manhattan Beach

Paragraph 51

A. OPTION(S) TO EXTEND:

Lessor hereby grants to Lessee the option to extend the term of this Lease for two (2) additional sixty (60) month period(s) commencing when the prior term expires upon each and all of the following terms and conditions:

(i) In order to exercise an option to extend, Lessee must give written notice of such election to Lessor and Lessor must receive the same at least 6

but not more than 12 months prior to the date that the option period would commence, time being of the essence. If proper notification of the exercise of an option is not given and/or received, such option shall automatically expire. Options (if there are more than one) may only be exercised consecutively.

(ii) The provisions of paragraph 39, including those relating to Lessee's Default set forth in paragraph 39.4 of this Lease, are conditions of this Option.

(iii) Except for the provisions of this Lease granting an option or options to extend the term, all of the terms and conditions of this Lease except where specifically modified by this option shall apply.

(iv) This Option is personal to the original Lessee, and cannot be assigned or exercised by anyone other than said original Lessee and only while the original Lessee is in full possession of the Premises and without the intention of thereafter assigning or subletting.

(v) The monthly rent for each month of the option period shall be calculated as follows, using the method(s) indicated below: (Check Method(s) to be Used and Fill in Appropriately)

[ ] II. Market Rental Value Adjustment(s) (MRV)

a. On (Fill in MRV Adjustment Date(s)) May 2, 2005 and May 2, 2010 the Base Rent shall be adjusted to the "Market Rental Value" of the property as follows:

1) Four months prior to each Market Rental Value Adjustment Date described above, the Parties shall attempt to agree upon what the new MRV will be on the adjustment date. If agreement cannot be reached, within thirty days, then:

(a) Lessor and Lessee shall immediately appoint a mutually acceptable appraiser or broker to establish the new MRV within the next thirty days. Any associated costs will be split equally between the Parties, or

(b) Both Lessor and Lessee shall each immediately make a reasonable determination of the MRV and submit such determination, in writing, to arbitration in accordance with the following provisions:

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(i) Within fifteen days thereafter, Lessor and Lessee shall each select an [ ] appraiser or [X] broker ("Consultant" - check one) of their choice to act as an arbitrator. The two arbitrators so appointed shall immediately select a third mutually acceptable Consultant to act as a third arbitrator.

(ii) The three arbitrators shall within thirty days of the appointment of the third arbitrator reach a decision as to what the actual MRV for the Premises is, and whether Lessor's or Lessee's submitted MRV is the closest thereto. The decision of a majority of the arbitrators shall be binding on the Parties. The submitted MRV which is determined to be the closest to the actual MRV shall thereafter be used by the Parties.

(iii) If either of the Parties fails to appoint an arbitrator within the specified fifteen days, the arbitrator timely appointed by one of them shall reach a decision on his or her own, and said decision shall be binding on the Parties.

(iv) The entire cost of such arbitration shall be paid by the party whose submitted MRV is not selected, ie. the one that is NOT the closest to the actual MRV.

2) Notwithstanding the foregoing, the new MRV shall not be less than the rent payable for the month immediately preceding the rent adjustment.

b. Upon the establishment of each New Market Rental Value:

1) the new MRV will become the new "Base Rent" for the purpose of calculating any further Adjustments, and

2) the first month of each Market Rental Value term shall become the new "Base Month" for the purpose of calculating any further Adjustments.

B. NOTICE:

Unless specified otherwise herein, notice of any rental adjustments, other than Fixed Rental Adjustments, shall be made as specified in paragraph 23 of the Lease.

C. BROKER'S FEE:

The Brokers specified in paragraph 1.10 shall be paid a Brokerage Fee for each adjustment specified above in accordance with paragraph 15 of the Lease.

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ADDENDUM TO STANDARD OFFICE LEASE-GROSS DATED NOVEMBER 18, 1999, BY AND BETWEEN PACIFICA CALIFORNIA/APOLLO, LLC, LESSOR, AND SKECHERS, INC., LESSEE FOR THE PREMISES LOCATED AT 225 S. SEPULVEDA BOULEVARD, MANHATTAN BEACH, CALIFORNIA.

This Addendum ("Addendum") is executed contemporaneously with that certain Standard Office Lease - ("Lease") by and between Lessor and Lessee, of even date herewith, respecting the Premises. Any conflict or ambiguity between this Addendum and the Lease shall be resolved in favor of this Addendum. Terms not otherwise defined herein shall have the meaning assigned to such terms in the Lease.

52. The Premises shall be deemed "Ready for Occupancy", and the Commencement Date shall be deemed the first (1st) business day after the Substantial Completion of the Tenant Improvements. The following dates in the Lease shall be extended by the number of days from and after the actual Commencement Date:

52.1 The "Expiration Date" in Paragraph 1.5 of the Lease, and wherever else in the Lease such term shall occur;

52.2 The "FRA Adjustment Date" in Paragraph 50 AIII of the Lease, and wherever else in the Lease such term shall occur;

52.3 The "MRV Adjustment Date" in Paragraph 51 AII of the Lease, and wherever else in the Lease such term shall occur;

53. INDEMNIFICATION: This Lease has been prepared by Leonard & Ohren, a California Corporation, at the request of Lessor and Lessee who are herein referred to as "the Parties" without regard to number or gender. The Parties have been advised to have this document reviewed by their own independent counsel, and confirm that in signing this document, they have not relied on any

acts or conduct of Leonard & Ohren, and its agents, with regard to the interpretation or meaning of this document. The Parties jointly and severally waive any and all claims, actions, demands, and loss against Leonard & Ohren, its agents, employees, and each of them, that a party may incur by reason of any act, error, or omission in the preparation of this document and in its interpretation and meaning, whether or not the interpretation or meaning is the result of compromise and settlement among Parties, or the result of determination by a court or arbitration panel of competent jurisdiction. The preceding waiver provisions have been negotiated by and between the Parties on the one part, and Leonard & Ohren on the other part.

54. ASSIGNMENT AND SUBLETTING - RECAPTURE OF PREMISES: At any time within thirty (30) days after Landlord's receipt of Tenant's proposed sublease, Landlord may by written notice to Tenant elect to (a) notify Tenant that it will not consent to the proposed subletting or assignment; (b) sublease the Premises or the portion thereof so proposed to be subleased by Tenant upon the same terms as those offered to the proposed subtenant; or (c) terminate this Lease as to the portion (including all) of the premises so proposed to be subleased or assigned, with a proportionate abatement in the rent payable hereunder. If Landlord does not exercise any option set forth in this Section 54 within said thirty (30) day period, Tenant may thereafter within ninety (90) days after the expiration of said thirty (30) day period enter into a valid assignment or sublease of the Premises or portion thereof, upon the terms and conditions set forth in the information [TEXT ILLEGIBLE] by Tenant to Landlord pursuant to Section [TEXT ILLEGIBLE]

55. LANDLORD'S SHARE OF PROFITS: If Tenant assigns or subleases, Tenant shall pay to Landlord as Additional Rent under the Lease the Landlord's fifty percent (50%) share of the Profit (defined below) on such transaction as and when received by Tenant, unless Landlord gives written notice to Tenant and the assignee or subtenant that Landlord's Share shall be paid by the assignee or subtenant to Landlord directly. The "Profit" means (A) all amounts paid to Tenant for such assignment or sublease, including "key" money, monthly rent in excess of the monthly rent payable under the Lease, and all fees and other consideration paid for the assignment or sublease, including fees under any collateral agreements, less (B) costs and expenses directly

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incurred by Tenant in connection with the execution and performance of such assignment or sublease for real estate broker's commissions and costs of renovation or construction of tenant improvements required under such assignment or sublease. Tenant is entitled to recover such costs and expenses before tenant is obligated to pay the Landlord's Share to Landlord.

56. RENTAL ABATEMENT: Landlord shall grant Tenant a rental abatement equal to the amount of four (4) month's rent for the first (1st) four (4) months of the term.

57. PARKING: Tenant shall be entitled to rent three (3) parking spaces per one thousand (1,000) square feet for the term of the Lease and any extension thereto at the building's prevailing rate. Tenant shall have the right to rent any additional spaces on an as-available month to month basis at the prevailing rate. The current prevailing rate is \$35 per car, per month. Included in the three (3) parking spaces per one thousand (1,000) square feet ratio, Tenant shall be entitled to rent nine (9) reserved parking spaces at building's unreserved prevailing rate which is currently \$35 per car, per month. Landlord shall grant Tenant four (4) months free rent for all parking.

58. RIGHT OF FIRST NEGOTIATION: Subject to availability, Tenant shall have the Right of First Negotiation to lease any additional forthcoming available space in the Building during the duration of the lease, including any option period. Landlord shall grant Tenant an opportunity to negotiate with Landlord ten (10) days prior to Landlord placing Premises on the market for lease.



59. SIGNAGE. Tenant shall be allowed to install building signage on the north end of the east facing side of the building. The size and design of the signage shall be subject to Landlord's approval and city or agency codes and restrictions.

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#### Exhibit "C"

#### TENANT WORK LETTER

This Tenant Work Letter, dated this 26th day of November, 1999, is entered into by and between Pacifica California/Apollo, LLC, a California limited liability company (hereinafter "Landlord") and Sketchers USA, Inc., a Delaware corporation (hereinafter "Tenant"). This Tenant Work Letter shall set forth the terms and conditions relating to the construction of Suites 125, 300 and 330 at Pacifica Manhattan Beach Office Plaza (hereinafter collectively, the "Premises"). This Tenant Work Letter is essentially organized chronologically and addresses the issues of the construction of the Premises, in sequence, as such issues will arise during the actual construction of the Premises. All references in this Tenant Work Letter to Articles or Sections of "this Lease" shall mean the relevant portions of Articles 1 through 49 of this Lease to which this Tenant Work Letter is attached as Exhibit "C", and all references in this Tenant Work Letter to Sections of "this Tenant Work Letter" shall mean the relevant portions of Sections 1 through 6 of this Tenant Work Letter.

#### SECTION 1

#### DELIVERY OF THE PREMISES AND BASE BUILDING

1.1 Base Building as Constructed by Landlord. Upon the full execution and delivery of this Lease by Landlord and Tenant, Landlord shall deliver the Premises to Tenant, and Tenant shall accept the Premises from Landlord in their presently existing, "as-is" condition. Tenant hereby warrants and represents that Tenant has inspected the Premises, is fully aware of the condition of the Premises, including demolition to be completed by Tenant, at Tenant's expense, prior to the construction of the Tenant Improvements by Tenant, and Tenant accepts such Premises in their present "as is" condition.

#### SECTION 2

#### TENANT IMPROVEMENTS

2.1 Tenant Improvement Allowance. Tenant shall be entitled to a one-time tenant improvement allowance (the "Tenant Improvement Allowance") in the amount of \$133,450.00 for the costs relating to the initial design and construction of Tenant's improvements, which are permanently affixed to the Premises (the "Tenant Improvements"). In no event shall Landlord be obligated to make disbursements pursuant to this Tenant Work Letter in a total amount which exceeds the Tenant Improvement Allowance, nor shall Landlord be obligated to expend the Tenant Improvement Allowance until such time as (i) all other sums required for the Tenant Improvements have been paid by or on behalf of Tenant, (ii) until Landlord shall receive, from all contractors,

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subcontractors, architects, designers, engineers and other individuals and entities employed by or on behalf of Tenant, involved in the design, development or construction of the Tenant Improvements, or in the delivery of materials utilized in the construction of the Tenant Improvements, lien releases on behalf of themselves, their employees and materialmen, conditional solely upon the payment of funds in the amount of the Tenant Improvement Allowance, and (iii), Landlord has previously deducted, from the Tenant Improvement Allowance a fee (the "Landlord Supervision Fee") in an amount equal to three percent (3%) of the total cost of the Tenant Improvements, including the Tenant Improvement Allowance.

2.2 Final Retention. Subject to the provisions of this Tenant Work Letter, a check for the Final Retention payable jointly to Tenant and Contractor shall be delivered by Landlord to Tenant following the completion of construction of the Premises, provided that (i) Tenant delivers to Landlord properly executed mechanics lien releases in compliance with both California Civil Code Section 3262(d)(2) and either Section 3262(d)(3) or Section 3262(d)(4), (ii) Landlord has determined that no substandard work exists which adversely affects the mechanical, electrical, plumbing, heating, ventilating and air conditioning, life-safety or other systems of the Building, the curtain wall of the Building, the structure or exterior appearance of the Building, or any other tenant's use of such other tenant's leased premises in the Building and (iii) Architect delivers to Landlord a certificate, in a form reasonably acceptable to Landlord, certifying that the construction of the Tenant Improvements in the Premises has been substantially completed.

2.3 Standard Tenant Improvement Package. Landlord has established specifications (the "Specifications") for the Building standard components to be used in the construction of the Tenant Improvements in the Premises (collectively, the "Standard Improvement Package"). The quality of Tenant Improvements shall be equal to or of greater quality than the quality of the Specifications, provided that the Tenant Improvements shall comply with certain Specifications as designated by Landlord. Landlord may make changes to the Specifications for the Standard Improvement Package from time to time.

### SECTION 3

#### CONSTRUCTION DRAWINGS

3.1 Selection of Drawings. Tenant shall retain an architect/space planner approved by Landlord (the "Architect") to prepare the Construction Drawings. Tenant shall retain the engineering consultants approved by Landlord (the "Engineers") to prepare all plans and engineering working drawings relating to the structural, mechanical, electrical, plumbing, HVAC, lifesafety, and sprinkler work in the Premises, which work is not part of the Base Building. The plans and drawings to be prepared by Architect and the Engineers hereunder shall be known collectively as the "Construction Drawings." All Construction Drawings shall comply with the drawing format and specifications determined by Landlord, and shall be subject to Landlord's approval, which Construction Drawings shall contain the information listed on Schedule 1, attached hereto. Tenant and Architect shall verify, in the field, the dimensions and conditions as shown on the relevant portions of the base building

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plans, and Tenant and Architect shall be solely responsible for the same, and Landlord shall have no responsibility in connection therewith. Landlord's review of the Construction Drawings as set forth in this Section 3, shall be for its sole purpose and shall not imply Landlord's review of the same, or obligate Landlord to review the same, for quality, design, Code compliance or other like matters. Accordingly, notwithstanding that any Construction Drawings are reviewed by Landlord or its space planner, architect, engineers and consultants, and notwithstanding any advice or assistance which may be rendered to Tenant by Landlord or Landlord's space planner, architect, engineers, and consultants, Landlord shall have no liability whatsoever in connection therewith and shall not be responsible for any omissions or errors contained in the Construction Drawings, and Tenant's waiver and indemnity set forth in Sections 8.7 and 8.8 of this Lease shall specifically apply to the Construction Drawings.

3.2 Final Space Plan. Tenant shall supply Landlord with four (4) copies signed by Tenant of its final space plan for the Premises before any architectural working drawings or engineering drawings have been commenced. The final space plan (the "Final Space Plan") shall include a layout and designation of all offices, rooms and other partitioning, their intended use, and equipment to be contained therein. Landlord may request clarification or

more specific drawings for special use items not included in the Final Space Plan. Landlord shall advise Tenant within five (5) business days after Landlord's receipt of the Final Space Plan for the Premises if the same is unsatisfactory or incomplete in any respect. If Tenant is so advised, Tenant shall promptly cause the Final Space Plan to be revised to correct any deficiencies or other matters Landlord may reasonably require.

3.3 Final Working Drawings. After the Final Space Plan has been approved by Landlord, Tenant shall supply the Engineers with a complete listing of standard and non-standard equipment and specifications, including, without limitation, B.T.U. calculations, electrical requirements and special electrical receptacle requirements for the Premises, to enable the Engineers and the Architect to complete the "Final Working Drawings" (as that term is defined below) in the manner as set forth below. Upon the approval of the Final Space Plan by Landlord and Tenant, Tenant shall promptly cause the Architect and the Engineers to complete the architectural and engineering drawings for the Premises, and Architect shall compile a fully coordinated set of architectural, structural, mechanical, electrical and plumbing working drawings in a form which is complete to allow subcontractor to bid on the work and to obtain all applicable permits (collectively, the "Final Working Drawings") and shall submit the same to Landlord for Landlord's approval. Tenant shall supply Landlord with four (4) copies signed by Tenant of such Final Working Drawings. Landlord shall advise Tenant within ten (10) business days after Landlord's receipt of the Final Working Drawings for the Premises if the same is unsatisfactory or incomplete in any respect. If Tenant is so advised, Tenant shall immediately revise the Final Working Drawings in accordance with such review and any disapproval of Landlord in connection therewith.

3.4 Approved Working Drawings. The Final Working Drawings shall be approved by Landlord (the "Approved Working Drawings") prior to the commencement of construction of the Premises by Tenant. After approval by Landlord of the Final Working Drawings, Tenant may submit the same to the City of Manhattan Beach for all applicable building permits. Tenant hereby agrees that neither Landlord nor Landlord's consultants shall be responsible for obtaining any building permit or certificate of occupancy for the Premises and that obtaining the same shall be Tenant's

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responsibility; provided, however, that Landlord shall cooperate with Tenant in executing permit applications and performing other ministerial acts reasonably necessary to enable Tenant to obtain any such permit or certificate of occupancy. No changes, modifications or alterations in the Approved Working Drawings may be made without the prior written consent of Landlord, which consent may not be unreasonably withheld.

#### SECTION 4

##### CONSTRUCTION OF THE TENANT IMPROVEMENTS

###### 4.1 Tenant's Selection of Contractors.

4.1.1 The Contractor. A general contractor shall be retained by Tenant to construct the Tenant Improvements. Such general contractor ("Contractor") shall be selected by Tenant and approved by Landlord, and Tenant shall deliver to Landlord notice of its selection of the Contractor upon such selection.

4.1.2 Tenant's Agents. All subcontractors, laborers, materialmen, and suppliers used by Tenant (such subcontractors, laborers, materialmen, and suppliers, and the Contractor to be known collectively as "Tenant's Agents") must be approved in writing by Landlord, which approval shall not be unreasonably withheld or delayed. If Landlord does not approve any

of Tenant's proposed subcontractors, laborers, materialmen or suppliers, Tenant shall submit other proposed subcontractors, laborers, materialmen or suppliers for Landlord's written approval. Notwithstanding the foregoing, Tenant shall retain subcontractors designated by Landlord in connection with any structural, mechanical, electrical, plumbing or heating, air-conditioning or ventilation work to be performed in the Premises.

#### 4.2 Construction of Tenant Improvements by Tenant's Agents.

4.2.1 Construction Contract; Cost Budget. Prior to Tenant's execution of the construction contract and general conditions with Contractor (the "Contract"), Tenant shall submit the Contract to Landlord for its approval, which approval shall not be unreasonably withheld or delayed. Prior to the commencement of the construction of the Tenant Improvements, and after Tenant has accepted all bids for the Tenant Improvements, Tenant shall provide Landlord with a detailed breakdown, by trade, of the final costs to be incurred or which have been incurred in connection with the design and construction of the Tenant Improvements to be performed by or at the direction of Tenant or the Contractor, which costs form a basis for the amount of the Contract (the "Final Costs"). Prior to the commencement of construction of the Tenant Improvements, Tenant shall deliver to Landlord, evidence reasonably satisfactory to Landlord that Tenant has available funds, in the form of cash or commitments to lend by a third party lender, in an amount (the "Over-Allowance Amount") equal to the difference between the amount of the Final Costs and the amount of the Tenant Improvement Allowance. In the event that, after the Final Costs have been determined, the costs relating to the design and construction of the Tenant Improvements shall change, any

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additional costs necessary to such design and construction in excess of the Final Costs, shall be paid by Tenant.

#### 4.2.2 Tenant's Agents.

4.2.2.1 Landlord's General Conditions for Tenant's Agents and Tenant Improvement Work. Tenant's and Tenant's Agent's construction of the Tenant Improvements shall comply with the following: (i) the Tenant Improvements shall be constructed in strict accordance with the Approved Working Drawings; (ii) Tenant's Agents shall submit schedules of all work relating to the Tenant's Improvements to Contractor and Contractor shall, within five (5) business days of receipt thereof, inform Tenant's Agents of any changes which are necessary thereto, and Tenant's Agents shall adhere to such corrected schedule; and (iii) Tenant shall abide by all rules made by Landlord's Building manager with respect to the use of elevators, storage of materials, coordination of work with the contractors of other tenants, and any other matter in connection with this Tenant Work Letter, including, without limitation, the construction of the Tenant Improvements.

4.2.2.2 Indemnity. Tenant's indemnity of Landlord as set forth in Sections 8.7 and 8.8 of this Lease shall also apply with respect to any and all costs, losses, damages, injuries and liabilities related in any way to any act or omission of Tenant or Tenant's Agents, or anyone directly or indirectly employed by any of them, or in connection with Tenant's non-payment of any amount arising out of the Tenant Improvements and/or Tenant's disapproval of all or any portion of any request for payment. Such indemnity by Tenant, as set forth in Sections 8.7 and 8.8 of this Lease, shall also apply with respect to any and all costs, losses, damages, injuries and liabilities related in any way to Landlord's performance of any ministerial acts reasonably necessary (i) to permit Tenant to complete the Tenant Improvements, and (ii) to enable Tenant to obtain any building permit or certificate of occupancy for the Premises.

4.2.2.3 Requirements of Tenant's Agents. Each of Tenant's Agents shall guarantee to Tenant and for the benefit of Landlord that the portion of the Tenant Improvements for which it is responsible shall be free from any

defects in workmanship and materials for a period of not less than one (1) year from the date of completion thereof. Each of Tenant's Agents shall be responsible for the replacement or repair, without additional charge, of all work done or furnished in accordance with its contract that shall become defective within one (1) year after the later to occur of (i) completion of the work performed by such contractor or subcontractors and (ii) the Lease Commencement Date. The correction of such work shall include, without additional charge, all additional expenses and damages incurred in connection with such removal or replacement of all or any part of the Tenant Improvements, and/or the Building and/or common areas that may be damaged or disturbed thereby. All such warranties or guarantees as to materials or workmanship of or with respect to the Tenant Improvements shall be contained in the Contract or subcontract and shall be written such that such guarantees or warranties shall inure to the benefit of both Landlord and Tenant, as their respective interests may appear, and can be directly enforced by either. Tenant covenants to give to Landlord any assignment or other assurances which may be necessary to effect such right of direct enforcement.

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#### 4.2.2.4 Insurance Requirements.

4.2.2.4.1 General Coverages. All of Tenant's Agents shall carry worker's compensation insurance covering all of their respective employees, and shall also carry public liability insurance, including property damage, all with limits, in form and with companies as are required to be carried by Tenant as set forth in Article 8 of this Lease.

4.2.2.4.2 Special Coverages. Tenant shall carry insurance in an amount, with terms reasonably approved by Landlord, either as an endorsement of Tenant's premises insurance or as a separate policy, at Tenant's election, covering the construction of the Tenant Improvements, and such other insurance as Landlord may require, it being understood and agreed that the Tenant Improvements shall be insured by Tenant pursuant to Article 8 of this Lease immediately upon completion thereof. Such insurance shall be in amounts and shall include such extended coverage endorsements as may be reasonably required by Landlord, each in amounts not less than \$500,000 per incident, \$1,000,000 in aggregate, and in form and with companies as are required to be carried by Tenant as set forth in Article 8 of this Lease.

4.2.2.4.3 General Terms. Certificates for all insurance carried pursuant to this Section 4.2.2.4 shall be delivered to Landlord before the commencement of construction of the Tenant Improvements and before the Contractor's equipment is moved onto the site. All such policies of insurance must contain a provision that the company writing said policy will give Landlord thirty (30) days' prior written notice of any cancellation or lapse of the effective date or any reduction in the amounts of such insurance. In the event that the Tenant Improvements are damaged by any cause during the course of the construction thereof, Tenant shall immediately repair the same at Tenant's sole cost and expense. Tenant's Agents shall maintain all of the foregoing insurance coverage in force until the Tenant Improvements are fully completed and accepted by Landlord. All policies carried under this Section 4.2.2.4 shall insure Landlord and Tenant, as their interests may appear, as well as Contractor and Tenant's Agents. All insurance, except Workers' Compensation, maintained by Tenant's Agents shall preclude subrogation claims by the insurer against anyone insured thereunder. Such insurance shall provide that it is primary insurance as respects the Landlord and that any other insurance maintained by Landlord is excess and noncontributing with the insurance required hereunder. The requirements for the foregoing insurance shall not derogate from the provisions for indemnification of Landlord by Tenant under Section 4.2.2.2 of this Tenant Work Letter.

4.2.3 Governmental Compliance. The Tenant Improvements shall comply in all respects with the following: (i) the Code and other state, federal, city or quasi-governmental laws, codes, ordinances and regulations, as each may apply according to the rulings of the controlling public official, agent or other

person; (ii) applicable standards of the American Insurance Association (formerly, the National Board of Fire Underwriters) and the National Electrical Code; and (iii) building material manufacturer's specifications.

4.2.4 Inspection by Landlord. Landlord shall have the right to inspect the Tenant Improvements at all times, provided however, that Landlord's failure to inspect the Tenant

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Improvements shall in no event constitute a waiver of any of Landlord's rights hereunder nor shall Landlord's inspection of the Tenant Improvements constitute Landlord's approval of the same. Should Landlord disapprove any portion of the Tenant's Improvements, Landlord shall notify Tenant in writing of such disapproval and shall specify the items disapproved. Any defects or deviations in, and/or disapproval by Landlord of, the Tenant Improvements shall be rectified by Tenant at no expense to Landlord, provided however, that in the event Landlord determines that a defect or deviation exists or disapproves of any matter in connection with any portion of the Tenant Improvements and such defect, deviation or matter might adversely affect the mechanical, electrical, plumbing, heating, ventilating and air-conditioning or life-safety systems of the Building, the structure or exterior appearance of the Building or any other tenant's use of such other tenant's leased premises, Landlord may take such action as Landlord deems necessary, at Tenant's expense and without incurring any liability on Landlord's part, to correct any such defect, deviation and/or matter, including, without limitation, causing the cessation of performance of the construction of the Tenant Improvements until such time as the defect, deviation and/or matter is corrected to Landlord's satisfaction.

4.3 Notice of Completion; Copy of Record Set of Plans. Within ten (10) days after completion of construction of the Tenant Improvements, Tenant shall cause a Notice of Completion to be recorded in the office of the Recorder of the County of Los Angeles in accordance with Section 3093 of the Civil Code of the State of California or any successor statute, and shall furnish a copy thereof to Landlord upon such recordation. If Tenant fails to do so, Landlord may execute and file the same on behalf of Tenant as Tenant's agent for such purpose, at Tenant's sole cost and expense. At the conclusion of construction, (i) Tenant shall cause the Architect and Contractor (A) to update the Approved Working Drawings as necessary to reflect all changes made to the Approved Working Drawings during the course of construction, (B) to certify to the best of their knowledge that the "record-set" of mylar as-built drawings are true and correct, which certification shall survive the expiration or termination of this Lease, and (C) to deliver to Landlord two (2) sets of copies of such record set of drawings within ninety (90) days following issuance of a certificate of occupancy for the Premises, and (ii) Tenant shall deliver to Landlord a copy of all warranties, guaranties, and operating manuals and information relating to the improvements, equipment, and systems in the Premises.

SECTION 5

COMPLETION OF THE TENANT IMPROVEMENTS:  
LEASE COMMENCEMENT DATE

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5.1 Except as provided in this Section 5, the Lease Commencement Date shall occur as set forth in the Amendment to Lease. The Lease Commencement Date shall be the earlier of (i) March 1, 2000, and (ii) the date Lessee first occupies the Premises for the purpose of conducting Lessee's business therein.

SECTION 6

MISCELLANEOUS

6.1 Tenant's Representative. Tenant shall designate an individual as its sole representative with respect to the matters set forth in this Tenant Work Letter, who shall have full authority and responsibility to act on behalf of the Tenant as required in this Tenant Work Letter. Upon such designation, Tenant shall identify such individual to Landlord, including such individual's address and telephone number.

6.2 Landlord's Representative. Landlord has designated both Clifford W. Lord, Jr. and Andy Carpiac, either one acting alone, as its representatives with respect to the matters set forth in this Tenant Work Letter, who, until further notice to Tenant, shall have full authority and responsibility to act on behalf of the Landlord as required in this Tenant Work Letter.

6.3 Time of the Essence in This Tenant Work Letter. Unless otherwise indicated, all references herein to a "number of days" shall mean and refer to calendar days. If any item requiring approval is timely disapproved by Landlord, the procedure for preparation of the document and approval thereof shall be repeated until the document is approved by Landlord. Landlord and Tenant expressly understand that time is of the essence and that any aspect of this Work Letter requiring Landlord's or Tenant's review and/or approval requires prompt review and/or approval.

6.4 Tenant's Lease Default. Notwithstanding any provision to the contrary contained in this Lease, if an event of default as described in Section 13 of Lease or this Tenant Work Letter has occurred at any time on or before the Substantial Completion of the Premises, then (i) in addition to all other rights and remedies granted to Landlord pursuant to this Lease, Landlord shall have the right to withhold payment of all or any portion of the Tenant Improvement Allowance until such time as the default is cured (provided such default is curable pursuant to the terms of the Lease) and/or Landlord may cause Contractor to cause the construction of the Premises (in which case, Tenant shall be responsible for any delay in the substantial completion of the Premises caused by such work stoppage), and (ii) all other obligations of Landlord under the terms of this Tenant Work Letter shall be forgiven until such time as such default is cured pursuant to the terms of this Lease (in which case, Tenant shall be responsible for any delay in the substantial completion of the Premises caused by such inaction by Landlord).

6.5 Tenant's Agents. All subcontractors, laborers, materialmen, and suppliers retained directly by Tenant shall conduct their activities in and around the Premises, Building and the Real Property in a harmonious relationship with all other subcontractors, laborers, materialmen and

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suppliers at the Premises, Building and Real Property, and, if necessary, Tenant shall employ union labor to achieve such harmonious relations.

6.6 Hazardous Materials. If the construction of the Tenant Improvements or Tenant's move into the Premises will involve the use of or disturb hazardous materials or substances existing in the Premises, Tenant shall comply with Landlord's rules and regulations concerning such hazardous materials or substances.

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SCHEDULE 1

Construction Drawings Showing

1. Location and type of all partitions.
2. Location and type of all doors. Indicate hardware and provide keying schedule.
3. Location and type of glass partitions, windows, and doors. Indicate framing and reference full-height partitions.
4. Locations of telephone equipment room.
5. Critical dimensions necessary for construction, with indication of required clearances.
6. Location and types of all electrical items: outlets, switches, telephone outlets and lighting.
7. Location and type of equipment that will require special electrical requirements. Provide manufacturers' specifications for use and operation, including heat output.
8. Location, weight per square foot, and description of any heavy equipment or filing system.
9. Requirements for special air-conditioning or ventilation.
10. Location and type of plumbing.
11. Location and type of kitchen equipment.
12. Location, type and color of floor covering, wall covering, paint and finishes. Details Showing:
  1. All millwork with verified dimensions of all equipment to be built in.
  2. Corridor entrance.
  3. Bracing or support of special walls, glass partitions, etc., if desired. If not included with the plans, Tenant's engineer will design all support or bracing required at Tenant's expense.

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Additional Information

1. Provide Landlord with Title 24 energy calculations.

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STANDARD INDUSTRIAL/COMMERCIAL MULTI-TENANT LEASE -- MODIFIED NET  
AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION

[AMERICAN INDUSTRIAL REAL ESTATE LOGO]

1. BASIC PROVISIONS ("BASIC PROVISIONS").

1.1 PARTIES: This Lease ("LEASE"), dated for reference purposes only, July 1, 1999, is made by and between Richard and Donna Piazza, Trustees of the Piazza Family Trust ("LESSOR") and Skechers U.S.A., Inc. ("LESSEE"), (collectively the "PARTIES," or individually a "PARTY").

1.2(a) PREMISES: That certain portion of the Building, including all improvements therein or to be provided by Lessor under the terms of this Lease, commonly known by the street address of 1108 B Manhattan Avenue, located in the City of Manhattan Beach, County of Los Angeles, State of California, with zip code 90266, as outlined on Exhibit \_\_\_\_ attached hereto ("PREMISES"). The "BUILDING" is that certain building containing the Premises and generally described as (describe briefly the nature of the Building): 1108-1112 Manhattan Avenue, Manhattan Beach, California.

In addition to Lessee's rights to use and occupy the Premises as hereinafter specified, Lessee shall have non-exclusive rights to the Common Areas (as defined in Paragraph 2.7 below) as hereinafter specified, but shall not have any rights to the roof, exterior walls or utility raceways of the Building or to any other buildings in the Industrial Center. The Premises, the Building, the Common Areas, the land upon which they are located, along with all other buildings and improvements thereon, are herein collectively referred to as the "INDUSTRIAL CENTER." (Also see Paragraph 2.)

1.2(b) PARKING: None unreserved vehicle parking spaces ("UNRESERVED PARKING SPACES"); and One (1) reserved vehicle parking spaces ("RESERVED PARKING SPACES"). (Also see Paragraph 2.6.)

1.3 TERM: 2 years and 8 months ("ORIGINAL TERM") commencing July 1, 1999 ("COMMENCEMENT DATE") and ending February 28, 2002 ("EXPIRATION DATE"). (Also see Paragraph 3.) See Paragraph 49.

1.4 EARLY POSSESSION: None ("EARLY POSSESSION DATE"). (Also see Paragraphs 3.2 and 3.3.)

1.5 BASE RENT: \$2,709.00 per month ("BASE RENT"), payable on the first day of each month commencing July 1, 1999 (Also see Paragraph 4.)

[X] If this box is checked, this Lease provides for the Base Rent to be adjusted per Addendum Paragraph 50, attached hereto. See Paragraph 50.

1.6(a) BASE RENT PAID UPON EXECUTION: \$2,709.00 as Base Rent for the period July 1 through July 31, 1999.

1.6(b) LESSEE'S SHARE OF COMMON AREA OPERATING EXPENSES: Ten and one-half percent (10 1/2%) ("LESSEE'S SHARE") as determined by [X] prorata square footage of the Premises as compared to the total square footage of the Building or [ ] other criteria as described in Addendum \_\_\_\_\_.

1.7 SECURITY DEPOSIT: \$-0- ("SECURITY DEPOSIT"). (Also see Paragraph 5.)

1.8 PERMITTED USE: General office use as per City Ordinance. ("PERMITTED USE") (Also see Paragraph 6.)

1.9 INSURING PARTY. Lessor is the "INSURING PARTY." (Also see Paragraph 8.)

1.10(a) REAL ESTATE BROKERS. The following real estate broker(s) (collectively, the "BROKERS") and brokerage relationships exist in this transaction and are consented to by the Parties (check applicable boxes):

- N/A represents Lessor exclusively ("LESSOR'S BROKER");
- N/A represents Lessee exclusively ("LESSEE'S BROKER"); or
- N/A represents both Lessor and Lessee ("DUAL AGENCY"). (Also see Paragraph 15.)

1.10(b) PAYMENT TO BROKERS. Upon the execution of this Lease by both Parties, Lessor shall pay to said Broker(s) jointly, or in such separate shares as they may mutually designate in writing, a fee as set forth in a separate written agreement between Lessor and said Broker(s) (or in the event there is no separate written agreement between Lessor and said Broker(s), the sum of \$-0-) for brokerage services rendered by said Broker(s) in connection with this transaction.

1.11 GUARANTOR. The obligations of the Lessee under this Lease are to be guaranteed by None ("GUARANTOR"). (Also see Paragraph 37.)

1.12 ADDENDA AND EXHIBITS. Attached hereto is an Addendum or Addenda consisting of Paragraphs 49 through 57, and Exhibits \_\_\_\_\_ through \_\_\_\_\_, all of which constitute a part of this Lease.

## 2. PREMISES, PARKING AND COMMON AREAS.

2.1 LETTING. Lessor hereby leases to Lessee, and Lessee hereby leases from Lessor, the Premises, for the term, at the rental, and upon all of the terms, covenants and conditions set forth in this Lease. Unless otherwise provided herein, any statement of square footage set forth in this Lease, or that may have been used in calculating rental and/or Common Area Operating Expenses, is an approximation which Lessor and Lessee agree is reasonable and the rental and Lessee's Share (as defined in Paragraph 1.6(b)) based thereon is not subject to revision whether or not the actual square footage is more or less.

2.4 ACCEPTANCE OF PREMISES. Lessee hereby acknowledges: (a) that it has been advised by the Broker(s) to satisfy itself with respect to the condition of the Premises (including, but not limited to, the electrical and fire sprinkler systems, security, environmental aspects, seismic and earthquake requirements, and compliance with the Americans with Disabilities Act and applicable zoning, municipal, county, state and federal laws, ordinances and regulations, and any covenants or restrictions of record (collectively, "APPLICABLE LAWS") and the present and future suitability of the Premises for Lessee's intended use; (b) that Lessee has made such investigation as it deems necessary with reference to such matters, is satisfied with reference thereto, and assumes all responsibility therefore as the same relate to Lessee's occupancy of the Premises and/or the terms of this Lease; and (c) that neither Lessor, nor any of Lessor's agents, has made any oral or written representations or warranties with respect to said matters other than as set forth in this Lease.

2.5 LESSEE AS PRIOR OWNER/OCCUPANT. The warranties made by Lessor in this Paragraph 2 shall be of no force or effect if immediately prior to the date set forth in Paragraph 1.1 Lessee was the owner or occupant of the Premises. In such event, Lessee shall, at Lessee's sole cost and expense, correct any non-compliance of the Premises with said warranties.

2.7 COMMON AREAS -- DEFINITION. The term "COMMON AREAS" is defined as all areas and facilities outside the Premises and within the exterior boundary line of the Industrial Center and interior utility raceways within the Premises that are provided and designated by the Lessor from time to time for the general nonexclusive use of Lessor, Lessee and other lessees of the Industrial Center

and their respective employees, suppliers, shippers, customers, contractors and invitees, including parking areas, loading and unloading areas, trash areas, roadways, sidewalks, walkways, parkways, driveways and landscaped areas.

2.8 COMMON AREAS -- LESSEE'S RIGHTS. Lessor hereby grants to Lessee, for the benefit of Lessee and its employees, suppliers, shippers, contractors, customers and invitees, during the term of this Lease, the non-exclusive right to use, in common with others entitled to such use, the Common Areas as they exist from time to time, subject to any rights, powers, and privileges reserved by Lessor under the terms hereof or under the terms of any rules and regulations or restrictions governing the use of the Industrial Center. Under no circumstances shall the right herein granted to use the Common Areas be deemed to include the right to store any property, temporarily or permanently, in the Common Areas. Any such storage shall be permitted only by the prior written consent of Lessor or Lessor's designated agent, which consent may be revoked at any time. In the event that any unauthorized storage shall occur then Lessor shall have the right, without notice, in addition to such other rights and remedies that it may have, to remove the property and charge the cost to Lessee, which cost shall be immediately payable upon demand by Lessor.

2.9 COMMON AREAS -- RULES AND REGULATIONS. Lessor or such other person(s) as Lessor may appoint shall have the exclusive control and management of the Common Areas and shall have the right, from time to time, to establish, modify, amend and enforce reasonable Rules and Regulations with respect thereto in accordance with Paragraph 40. Lessee agrees to abide by and conform to all such Rules and Regulations, and to cause its employees, suppliers, shippers, customers, contractors and invitees to so abide and conform. Lessor shall not be responsible to Lessee for the non-compliance with said rules and regulations by other lessees of the Industrial Center.

2.10 COMMON AREAS -- CHANGES. Lessor shall have the right, in Lessor's sole discretion, from time to time:

(a) To make changes to the Common Areas, including, without limitation, changes in the location, size, shape and number of driveways, entrances, parking spaces, parking areas, loading and unloading areas, ingress, egress, direction of traffic, landscaped areas, walkways and utility raceways;

(b) To close temporarily any of the Common Areas for maintenance purposes so long as reasonable access to the Premises remains available;

(c) To designate other land outside the boundaries of the Industrial Center to be a part of the Common Areas;

(d) To add additional buildings and improvements to the Common Areas;

(e) To use the Common Areas while engaged in making additional improvements, repairs or alterations to the Industrial Center, or any portion thereof; and

(f) To do and perform such other acts and make such other changes in, to or with respect to the Common Areas and Industrial Center as Lessor may, in the exercise of sound business judgment, deem to be appropriate.

### 3. TERM.

3.1 TERM. The Commencement Date, Expiration Date and Original Term of this Lease are as specified in Paragraph 1.3.

### 4. RENT.

4.1 BASE RENT. Lessee shall pay Base Rent and other rent or charges, as the same may be adjusted from time to time, to Lessor in lawful money of the United States, without offset or deduction, on or before the day on which it is due under the terms of this Lease. Base Rent and all other rent and charges for any period during the term hereof which is for less than one full month shall be prorated based upon the actual number of days of the month involved. Payment of

Base Rent and other charges shall be made to Lessor at its address stated herein or to such other persons or at such other addresses as Lessor may from time to time designate in writing to Lessee.

4.2 COMMON AREA OPERATING EXPENSES. Lessee shall pay to Lessor during the term hereof, in addition to the Base Rent, Lessee's Share (as specified in Paragraph 1.6(b)) of all Common Area Operating Expenses, as hereinafter defined, during each calendar year of the term of this Lease, in accordance with the following provisions:

(a) "COMMON AREA OPERATING EXPENSES" are defined, for purposes of this Lease, as all costs incurred by Lessor relating to the ownership and operation of the Industrial Center, including, but not limited to, the following:

(i) The operation, repair and maintenance, in neat, clean, good order and condition, of the following:

(aa) The Common Areas, including parking areas, loading and unloading areas, trash areas, roadways, sidewalks, walkways, parkways, driveways, landscaped areas, striping, bumpers, irrigation systems, Common Area lighting facilities, fences and gates, elevators and roof.

(bb) Exterior signs and any tenant directories.

(cc) Fire detection and sprinkler systems.

(ii) The cost of water, gas, electricity and telephone to service the Common Areas.

(iii) Trash disposal, property management and security services and the costs of any environmental inspections.

(v) Real Property Taxes (as defined in Paragraph 10.2) to be paid by Lessor for the Building and the Common Areas under Paragraph 10 hereof.

(vi) The costs of the premiums for the insurance policies maintained by Lessor under Paragraph 8 hereof.

(vii) Any deductible portion of an insured loss concerning the Building or the Common Areas.

(viii) Any other services to be provided by Lessor that are stated elsewhere in this Lease to be a Common Area Operating Expense.

(b) Any Common Area Operating Expenses and Real Property Taxes that are specifically attributable to the Building or to any other building in the Industrial Center or to the operation, repair and maintenance thereof, shall be allocated entirely to the Building or to such other building. However, any Common Area Operating Expenses and Real Property Taxes that are not specifically attributable to the Building or to any other building or to the operation, repair and maintenance thereof, shall be equitably allocated by Lessor to all buildings in the Industrial Center.

(c) The inclusion of the improvements, facilities and services set forth in Subparagraph 4.2(a) shall not be deemed to impose an obligation upon Lessor to either have said improvements or facilities or to provide those services unless the Industrial Center already has the same, Lessor already provides the services, or Lessor has agreed elsewhere in this Lease to provide the same or some of them.

(d) Lessee's Share of Common Area Operating Expenses shall be payable by Lessee within ten (10) days after a reasonably detailed statement of actual expenses is presented to Lessee by Lessor. At Lessor's option, however, an amount may be estimated by Lessor from time to time of Lessee's Share of annual Common Area Operating Expenses and the same shall be payable monthly or quarterly, as Lessor shall designate, during each 12-month period of the Lease term, on the same day as the Base Rent is due hereunder. Lessor shall deliver to

Lessee within sixty (60) days after the expiration of each calendar year a reasonably detailed statement showing Lessee's Share of the actual Common Area Operating Expenses incurred during the preceding year. If Lessee's payments under this Paragraph 4.2(d) during said preceding year exceed Lessee's Share as indicated on said statement, Lessee shall be credited the amount of such over

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payment against Lessee's Share of Common Area Operating Expenses next becoming due. If Lessee's payments under this Paragraph 4.2(d) during said preceding year were less than Lessee's Share as indicated on said statement, Lessee shall pay to Lessor the amount of the deficiency within ten (10) days after delivery by Lessor to Lessee of said statement. See Paragraphs 53 and 54.

5. SECURITY DEPOSIT. Lessee shall deposit with Lessor upon Lessee's execution hereof the Security Deposit set forth in Paragraph 1.7 as security for Lessee's faithful performance of Lessee's obligations under this Lease. If Lessee fails to pay Base Rent or other rent or charges due hereunder, or otherwise Defaults under this Lease (as defined in Paragraph 13.1), Lessor may use, apply or retain all or any portion of said Security Deposit for the payment of any amount due Lessor or to reimburse or compensate Lessor for any liability, cost, expense, loss or damage (including attorneys' fees) which Lessor may suffer or incur by reason thereof. If Lessor uses or applies all or any portion of said Security Deposit, Lessee shall within ten (10) days after written request therefore deposit monies with Lessor sufficient to restore said Security Deposit to the full amount required by this Lease. Any time the Base Rent increases during the term of this Lease, Lessee shall, upon written request from Lessor, deposit additional monies with Lessor as an addition to the Security Deposit so that the total amount of the Security Deposit shall at all times bear the same proportion to the then current Base Rent as the initial Security Deposit bears to the initial Base Rent set forth in Paragraph 1.5. Lessor shall not be required to keep all or any part of the Security Deposit separate from its general accounts. Lessor shall, at the expiration or earlier termination of the term hereof and after Lessee has vacated the Premises, return to Lessee (or, at Lessor's option, to the last assignee, if any, of Lessee's interest herein), that portion of the Security Deposit not used or applied by Lessor. Unless otherwise expressly agreed in writing by Lessor, no part of the Security Deposit shall be considered to be held in trust, to bear interest or other increment for its use, or to be prepayment for any monies to be paid by Lessee under this Lease.

6. USE.

6.1 PERMITTED USE.

(a) Lessee shall use and occupy the Premises only for the Permitted Use set forth in Paragraph 1.8, and for no other purpose. Lessee shall not use or permit the use of the Premises in a manner that is unlawful, creates waste or a nuisance, or that disturbs owners and/or occupants of, or causes damage to the Premises or neighboring premises or properties.

6.2 HAZARDOUS SUBSTANCES.

(a) REPORTABLE USES REQUIRE CONSENT. The term "HAZARDOUS SUBSTANCE" as used in this Lease shall mean any product, substance, chemical, material or waste whose presence, nature, quantity and/or intensity of existence, use, manufacture, disposal, transportation, spill, release or effect, either by itself or in combination with other materials expected to be on the Premises, is either: (i) potentially injurious to the public health, safety or welfare, the environment, or the Premises; (ii) regulated or monitored by any governmental authority; or (iii) a basis for potential liability of Lessor to any governmental agency or third party under any applicable statute or common law theory. Hazardous Substance shall include, but not be limited to, hydrocarbons, petroleum, gasoline, crude oil or any products or by-products thereof. Lessee shall not engage in any activity in or about the Premises which

constitutes a Reportable Use (as hereinafter defined) of Hazardous Substances without the express prior written consent of Lessor and compliance in a timely manner (at Lessee's sole cost and expense) with all Applicable Requirements (as defined in Paragraph 6.3). "REPORTABLE USE" shall mean (i) the installation or use of any above or below ground storage tank; (ii) the generation, possession, storage, use, transportation, or disposal of a Hazardous Substance that requires a permit from, or with respect to which a report, notice, registration or business plan is required to be filed with, any governmental authority; and (iii) the presence in, on or about the Premises of a Hazardous Substance with respect to which any Applicable Laws require that a notice be given to persons entering or occupying the Premises or neighboring properties. Notwithstanding the foregoing, Lessee may, without Lessor's prior consent, but upon notice to Lessor and in compliance with all Applicable Requirements, use any ordinary and customary materials reasonably required to be used by Lessee in the normal course of the Permitted Use, so long as such use is not a Reportable Use and does not expose the Premises or neighboring properties to any meaningful risk of contamination or damage or expose Lessor to any liability therefor. In addition, Lessor may (but without any obligation to do so) condition its consent to any Reportable Use of any Hazardous Substance by Lessee upon Lessee's giving Lessor such additional assurances as Lessor, in its reasonable discretion, deems necessary to protect itself, the public, the Premises and the environment against damage, contamination or injury and/or liability therefor, including, but not limited to, the installation (and, at Lessor's option, removal on or before Lease expiration or earlier termination) of reasonably necessary protective modifications to the Premises (such as concrete encasements) and/or the deposit of an additional Security Deposit under Paragraph 5 hereof.

(b) DUTY TO INFORM LESSOR. If Lessee knows, or has reasonable cause to believe, that a Hazardous Substance has come to be located in, on, under or about the Premises or the Building, other than as previously consented to by Lessor, Lessee shall immediately give Lessor written notice thereof, together with a copy of any statement, report, notice, registration, application, permit, business plan, license, claim, action, or proceeding given to, or received from, any governmental authority or private party concerning the presence, spill, release, discharge of, or exposure to, such Hazardous Substance including, but not limited to, all such documents as may be involved in any Reportable Use involving the Premises. Lessee shall not cause or permit any Hazardous Substance to be spilled or released in, on, under or about the Premises (including, without limitation, through the plumbing or sanitary sewer system).

(c) INDEMNIFICATION. Lessee shall indemnify, protect, defend and hold Lessor, its agents, employees, lenders and ground lessor, if any, and the Premises, harmless from and against any and all damages, liabilities, judgments, costs, claims, liens, expenses, penalties, loss of permits and attorneys' and consultants' fees arising out of or involving any Hazardous Substance brought onto the Premises by or for Lessee or by anyone under Lessee's control. Lessee's obligations under this Paragraph 6.2(c) shall include, but not be limited to, the effects of any contamination or injury to person, property or the environment created or suffered by Lessee, and the cost of investigation (including consultants' and attorneys' fees and testing), removal, remediation, restoration and/or abatement thereof, or of any contamination therein involved, and shall survive the expiration or earlier termination of this Lease. No termination, cancellation or release agreement entered into by Lessor and Lessee shall release Lessee from its obligations under this Lease with respect to Hazardous Substances, unless specifically so agreed by Lessor in writing at the time of such agreement.

6.3 LESSEE'S COMPLIANCE WITH REQUIREMENTS. Lessee shall, at Lessee's sole cost and expense, fully, diligently and in a timely manner, comply with all "APPLICABLE REQUIREMENTS," which term is used in this Lease to mean all laws, rules, regulations, ordinances, directives, covenants, easements and restrictions of record, permits, the requirements of any applicable fire insurance underwriter or rating bureau, and the recommendations of Lessor's engineers and/or consultants, relating in any manner to the Premises (including, but not limited to, matters pertaining to (i) industrial hygiene; (ii) environmental conditions on, in, under or about the Premises, including soil and groundwater conditions; and (iii) the use, generation, manufacture, production,

installation, maintenance, removal, transportation, storage, spill, or release of any Hazardous Substance), now in effect or which may hereafter come into effect. Lessee shall, within five (5) days after receipt of Lessor's written request, provide Lessor with copies of all documents and information, including, but not limited to, permits, registrations, manifests, applications, reports and certificates, evidencing Lessee's compliance with any Applicable Requirements specified by Lessor, and shall immediately upon receipt, notify Lessor in writing (with copies of any documents involved) of any threatened or actual claim, notice, citation, warning, complaint or report pertaining to or involving failure by Lessee or the Premises to comply with any Applicable Requirements.

6.4 INSPECTION; COMPLIANCE WITH LAW. Lessor, Lessor's agents, employees, contractors and designated representatives, and the holders of any mortgages, deeds of trust or ground leases on the Premises ("LENDERS") shall have the right to enter the Premises at any time in the case of an emergency, and otherwise at reasonable times, for the purpose of inspecting the condition of the Premises and for verifying compliance by Lessee with this Lease and all Applicable Requirements (as defined in Paragraph 6.3), and Lessor shall be entitled to employ experts and/or consultants in connection therewith to advise Lessor with respect to Lessee's activities, including but not limited to Lessee's installation, operation, use, monitoring, maintenance, or removal of any Hazardous Substance on or from the Premises. The costs and expenses of any such inspections shall be paid by the party requesting same, unless a Default or Breach of this Lease by Lessee or a violation of Applicable Requirements or a contamination, caused or materially contributed to by Lessee, is found to exist or to be imminent, or unless the inspection is requested or ordered by a governmental authority as the result of any such existing or imminent violation or contamination. In such case, Lessee shall upon request reimburse Lessor or Lessor's Lender, as the case may be, for the costs and expenses of such inspections.

#### 7. MAINTENANCE, REPAIRS, UTILITY INSTALLATIONS, TRADE FIXTURES AND ALTERATIONS.

##### 7.1 LESSEE'S OBLIGATIONS.

(a) Subject to the provisions of Paragraphs 7.2 (Lessor's Obligations), 9 (Damage or Destruction), and 14 (Condemnation), Lessee shall, at Lessee's sole cost and expense and at all times, keep the Premises and every part thereof in good order, condition and repair (whether or not such portion of the Premises requiring repair, or the means of repairing the same, are reasonably or readily accessible to Lessee, and whether or not the need for such repairs occurs as a result of Lessee's use, any prior use, the elements or the age of such portion of the Premises), including, without limiting the generality of the foregoing, all equipment or facilities specifically serving the Premises, such as plumbing, heating, air conditioning, ventilating, electrical, lighting facilities, boilers, fired or unfired pressure vessels, fire hose connections if within the Premises, fixtures, interior walls, interior surfaces of exterior walls, ceilings, floors, windows, doors, plate glass, and skylights, but excluding any items which are the responsibility of Lessor pursuant to Paragraph 7.2 below. Lessee, in keeping the Premises in good order, condition and repair, shall exercise and perform good maintenance practices. Lessee's obligations shall include restorations, replacements or renewals when necessary to keep the Premises and all improvements thereon or a part thereof in good order, condition and state of repair.

(c) If Lessee fails to perform Lessee's obligations under this Paragraph 7.1, Lessor may enter upon the Premises after ten (10) days' prior written notice to Lessee (except in the case of an emergency, in which case no notice shall be required), perform such obligations on Lessee's behalf, and put the Premises in good order, condition and repair, in accordance with Paragraph 13.2 below.

7.2 LESSOR'S OBLIGATIONS. Subject to the provisions of Paragraphs 4.2 (Common Area Operating Expenses), 6 (Use), 7.1 (Lessee's Obligations), 9 (Damage or Destruction) and 14 (Condemnation), Lessor, subject to reimbursement pursuant to Paragraph 4.2, shall keep in good order, condition and repair the foundations, exterior walls, structural condition of interior bearing walls,

exterior roof, fire sprinkler and/or standpipe and hose (if located in the Common Areas) or other automatic fire extinguishing system including fire alarm and/or smoke

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detection systems and equipment, fire hydrants, parking lots, walkways, parkways, driveways, landscaping, fences, signs and utility systems serving the Common Areas and all parts thereof, as well as providing the services for which there is a Common Area Operating Expense pursuant to Paragraph 4.2. Lessor shall not be obligated to paint the exterior or interior surfaces of exterior walls nor shall Lessor be obligated to maintain, repair or replace windows, doors or plate glass of the Premises. Lessee expressly waives the benefit of any statute now or hereafter in effect which would otherwise afford Lessee the right to make repairs at Lessor's expense or to terminate this Lease because of Lessor's failure to keep the Building, Industrial Center or Common Areas in good order, condition and repair.

### 7.3 UTILITY INSTALLATIONS, TRADE FIXTURES, ALTERATIONS.

(a) DEFINITIONS; CONSENT REQUIRED. The term "UTILITY INSTALLATIONS" is used in this Lease to refer to all air lines, power panels, electrical distribution, security, fire protection systems, communications systems, lighting fixtures, heating, ventilating and air conditioning equipment, plumbing, and fencing in, on or about the Premises. The term "TRADE FIXTURES" shall mean Lessee's machinery and equipment which can be removed without doing material damage to the Premises. The term "ALTERATIONS" shall mean any modification of the improvements on the Premises which are provided by Lessor under the terms of this Lease, other than Utility Installations or Trade Fixtures. "LESSEE-OWNED ALTERATIONS AND/OR UTILITY INSTALLATIONS" are defined as Alterations and/or Utility Installations made by Lessee that are not yet owned by Lessor pursuant to Paragraph 7.4(a). Lessee shall not make nor cause to be made any Alterations or Utility Installations in, on, under or about the Premises without Lessor's prior written consent. Lessee may, however, make non-structural Utility Installations to the interior of the Premises (excluding the roof) without Lessor's consent but upon notice to Lessor, so long as they are not visible from the outside of the Premises, do not involve puncturing, relocating or removing the roof or any existing walls, or changing or interfering with the fire sprinkler or fire detection systems and the cumulative cost thereof during the term of this Lease as extended does not exceed \$2,500.00.

(b) CONSENT. Any Alterations or Utility Installations that Lessee shall desire to make and which require the consent of the Lessor shall be presented to Lessor in written form with detailed plans. All consents given by Lessor, whether by virtue of Paragraph 7.3(a) or by subsequent specific consent, shall be deemed conditioned upon: (i) Lessee's acquiring all applicable permits required by governmental authorities; (ii) the furnishing of copies of such permits together with a copy of the plans and specifications for the Alteration or Utility Installation to Lessor prior to commencement of the work thereon; and (iii) the compliance by Lessee with all conditions of said permits in a prompt and expeditious manner. Any Alterations or Utility Installations by Lessee during the term of this Lease shall be done in a good and workmanlike manner, with good and sufficient materials, and be in compliance with all Applicable Requirements. Lessee shall promptly upon completion thereof furnish Lessor with as-built plans and specifications therefor. Lessor may (but without obligation to do so) condition its consent to any requested Alteration or Utility Installation that costs \$2,500.00 or more upon Lessee's providing Lessor with a lien and completion bond in an amount equal to one and one-half times the estimated cost of such Alteration or Utility Installation.

(c) LIEN PROTECTION. Lessee shall pay when due all claims for labor or materials furnished or alleged to have been furnished to or for Lessee at or for use on the Premises, which claims are or may be secured by any mechanic's or materialmen's lien against the Premises or any interest therein.



Lessee shall give Lessor not less than ten (10) days' notice prior to the commencement of any work in, on, or about the Premises, and Lessor shall have the right to post notices of non-responsibility in or on the Premises as provided by law. If Lessee shall, in good faith, contest the validity of any such lien, claim or demand, then Lessee shall, at its sole expense, defend and protect itself, Lessor and the Premises against the same and shall pay and satisfy any such adverse judgment that may be rendered thereon before the enforcement thereof against the Lessor or the Premises. If Lessor shall require, Lessee shall furnish to Lessor a surety bond satisfactory to Lessor, in an amount equal to one and one-half times the amount of such contested lien claim or demand, indemnifying Lessor against liability for the same, as required by law for the holding of the Premises free from the effect of such lien or claim. In addition, Lessor may require Lessee to pay Lessor's attorneys' fees and costs in participating in such action if Lessor shall decide it is to its best interest to do so.

#### 7.4 OWNERSHIP, REMOVAL, SURRENDER, AND RESTORATION.

(a) OWNERSHIP. Subject to Lessor's right to require their removal and to cause Lessee to become the owner thereof as hereinafter provided in this Paragraph 7.4, all Alterations and Utility Installations made to the Premises by Lessee shall be the property of and owned by Lessee, but considered a part of the Premises. Lessor may, at any time and at its option, elect in writing to Lessee to be the owner of all or any specified part of the Lessee-Owned Alterations and Utility Installations. Unless otherwise instructed per Subparagraph 7.4(b) hereof, all Lessee-Owned Alterations and Utility Installations shall, at the expiration or earlier termination of this Lease, become the property of Lessor and remain upon the Premises and be surrendered with the Premises by Lessee.

(b) REMOVAL. Unless otherwise agreed in writing, Lessor may require that any or all Lessee-Owned Alterations or Utility Installations be removed by the expiration or earlier termination of this Lease, notwithstanding that their installation may have been consented to by Lessor. Lessor may require the removal at any time of all or any part of any Alterations or Utility Installations made without the required consent of Lessor.

(c) SURRENDER/RESTORATION. Lessee shall surrender the Premises by the end of the last day of the Lease term or any earlier termination date, clean and free of debris and in good operating order, condition and state of repair, ordinary wear and tear excepted. Ordinary wear and tear shall not include any damage or deterioration that would have been prevented by good maintenance practice or by Lessee performing all of its obligations under this Lease. Except as otherwise agreed or specified herein, the Premises, as surrendered, shall include the Alterations and Utility Installations. The obligation of Lessee shall include the repair of any damage occasioned by the installation, maintenance or removal of Lessee's Trade Fixtures, furnishings, equipment, and Lessee-Owned Alterations and Utility Installations, as well as the removal of any storage tank installed by or for Lessee, and the removal, replacement, or remediation of any soil, material or ground water contaminated by Lessee, all as may then be required by Applicable Requirements and/or good practice. Lessee's Trade Fixtures shall remain the property of Lessee and shall be removed by Lessee subject to its obligation to repair and restore the Premises per this Lease.

#### 8. INSURANCE; INDEMNITY.

8.1 PAYMENT OF PREMIUMS. The cost of the premiums for the insurance policies maintained by Lessor under this Paragraph 8 shall be a Common Area Operating Expense pursuant to Paragraph 4.2 hereof. Premiums for policy periods commencing prior to, or extending beyond, the term of this Lease shall be prorated to coincide with the corresponding Commencement Date or Expiration Date.

#### 8.2 LIABILITY INSURANCE.

(a) CARRIED BY LESSEE. Lessee shall obtain and keep in force during the term of this Lease a Commercial General Liability policy of insurance

protecting Lessee, Lessor and any Lender(s) whose names have been provided to Lessee in writing (as additional insureds) against claims for bodily injury, personal injury and property damage based upon, involving or arising out of the ownership, use, occupancy or maintenance of the Premises and all areas appurtenant thereto. Such insurance shall be on an occurrence basis providing single limit coverage in an amount not less than \$1,000,000 per occurrence with an "Additional Insured-Managers or Lessors of Premises" endorsement and contain the "Amendment of the Pollution Exclusion" endorsement for damage caused by heat, smoke or fumes from a hostile fire. The policy shall not contain any intra-insured exclusions as between insured persons or organizations, but shall include coverage for liability assumed under this Lease as an "INSURED CONTRACT" for the performance of Lessee's indemnity obligations under this Lease. The limits of said insurance required by this Lease or as carried by Lessee shall not, however, limit the liability of Lessee nor relieve Lessee of any obligation hereunder. All insurance to be carried by Lessee shall be primary to and not contributory with any similar insurance carried by Lessor, whose insurance shall be considered excess insurance only.

(b) CARRIED BY LESSOR. Lessor shall also maintain liability insurance described in Paragraph 8.2(a) above, in addition to and not in lieu of, the insurance required to be maintained by Lessee. Lessee shall not be named as an additional insured therein.

### 8.3 PROPERTY INSURANCE - BUILDING, IMPROVEMENTS AND RENTAL VALUE.

(a) BUILDING AND IMPROVEMENTS. Lessor shall obtain and keep in force during the term of this Lease a policy or policies in the name of Lessor, with loss payable to Lessor and to any Lender(s), insuring against loss or damage to the Premises. Such insurance shall be for full replacement cost, as the same shall exist from time to time, or the amount required by any Lender(s), but in no event more than the commercially reasonable and available insurable value thereof if, by reason of the unique nature or age of the improvements involved, such latter amount is less than full replacement cost. Lessee-Owned Alterations and Utility Installations, Trade Fixtures and Lessee's personal property shall be insured by Lessee pursuant to Paragraph 8.4. If the coverage is available and commercially appropriate, Lessor's policy or policies shall insure against all risks of direct physical loss or damage (except the perils of flood and/or earthquake unless required by a Lender), including coverage for any additional costs resulting from debris removal and reasonable amounts of coverage for the enforcement of any ordinance or law regulating the reconstruction or replacement of any undamaged sections of the Building required to be demolished or removed by reason of the enforcement of any building, zoning, safety or land use laws as the result of a covered loss, but not including plate glass insurance. Said policy or policies shall also contain an agreed valuation provision in lieu of any co-insurance clause, waiver of subrogation, and inflation guard protection causing an increase in the annual property insurance coverage amount by a factor of not less than the adjusted U.S. Department of Labor Consumer Price Index for All Urban Consumers for the city nearest to where the Premises are located.

(b) RENTAL VALUE. Lessor may also obtain and keep in force during the term of this Lease a policy or policies in the name of Lessor, with loss payable to Lessor and any Lender(s), insuring the loss of the full rental and other charges payable by all lessees of the Building to Lessor for one year (including all Real Property Taxes, insurance costs, all Common Area Operating Expenses and any scheduled rental increases). Said insurance may provide that in the event the Lease is terminated by reason of an insured loss, the period of indemnity for such coverage shall be extended beyond the date of the completion of repairs or replacement of the Premises, to provide for one full year's loss of rental revenues from the date of any such loss. Said insurance shall contain an agreed valuation provision in lieu of any co-insurance clause, and the amount of coverage shall be adjusted annually to reflect the projected rental income, Real Property Taxes, insurance premium costs and other expenses, if any, otherwise payable, for the next 12-month period. Common Area Operating Expenses shall include any deductible amount in the event of such loss.

(c) ADJACENT PREMISES. Lessee shall pay for any increase in the premiums for the property insurance of the Building and for the Common Areas or

other buildings in the Industrial Center if said increase is caused by Lessee's acts, omissions, use or occupancy of the Premises.

(d) LESSEE'S IMPROVEMENTS. Since Lessor is the Insuring Party, Lessor shall not be required to insure Lessee-Owned Alterations and Utility Installations.

8.4 LESSEE'S PROPERTY INSURANCE. Subject to the requirements of Paragraph 8.5, Lessee at its cost shall either by separate policy or, at Lessor's option, by endorsement to a policy already carried, maintain insurance coverage on all of Lessee's personal property, Trade Fixtures and Lessee-Owned Alterations and Utility Installations in, on, or about the Premises similar in coverage to that carried by Lessor as the Insuring Party under Paragraph 8.3(a). Such insurance shall be full replacement cost coverage with a deductible not to exceed \$1,000 per occurrence. The proceeds from any such insurance shall be used by Lessee for the replacement of personal property and the restoration of Trade Fixtures and Lessee-Owned Alterations and Utility Installations. Upon request from Lessor, Lessee shall provide Lessor with written evidence that such insurance is in force.

8.5 INSURANCE POLICIES. Insurance required hereunder shall be in companies duly licensed to transact business in the state where the Premises are located, and maintaining during the policy term a "General Policyholders Rating" of at least B+, V, or such other rating as may be required by a Lender, as set forth in the most current issue of "Best's Insurance Guide." Lessee may be maintained by Lessee under a blanket policy or policies and shall not do or permit to be done anything which shall invalidate the insurance policies referred to in

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this Paragraph 8. Lessee shall cause to be delivered to Lessor, within seven (7) days after the earlier of the Early Possession Date or the Commencement Date, certified copies of, or certificates evidencing the existence and amounts of, the insurance required under Paragraph 8.2(a) and 8.4. No such policy shall be cancelable or subject to modification except after thirty (30) days' prior written notice to Lessor. Lessee shall, at least thirty (30) days prior to the expiration of such policies, furnish Lessor with evidence of renewals or "insurance binders" evidencing renewal thereof, or Lessor may order such insurance and charge the cost thereof to Lessee, which amount shall be payable by Lessee to Lessor upon demand.

8.6 WAIVER OF SUBROGATION. Without affecting any other rights or remedies, Lessee and Lessor each hereby release and relieve the other, and waive their entire right to recover damages (whether in contract or in tort) against the other, for loss or damage to their property arising out of or incident to the perils required to be insured against under Paragraph 8. The effect of such releases and waivers of the right to recover damages shall not be limited by the amount of insurance carried or required, or by any deductibles applicable thereto. Lessor and Lessee agree to have their respective insurance companies issuing property damage insurance waive any right to subrogation that such companies may have against Lessor or Lessee, as the case may be, so long as the insurance is not invalidated thereby.

8.7 INDEMNITY. Except for Lessor's negligence and/or breach of express warranties, Lessee shall indemnify, protect, defend and hold harmless the Premises, Lessor and its agents, Lessor's master or ground lessor, partners and Lenders, from and against any and all claims, loss of rents and/or damages, costs, liens, judgments, penalties, loss of permits, attorneys' and consultants' fees, expenses and/or liabilities arising out of, involving, or in connection with, the occupancy of the Premises by Lessee, the conduct of Lessee's business, any act, omission or neglect of Lessee, its agents, contractors, employees or invitees, and out of any Default or Breach by Lessee in the performance in a timely manner of any obligation on Lessee's part to be performed under this Lease. The foregoing shall include, but not be limited to, the defense or pursuit of any claim or any action or proceeding involved therein, and whether

or not (in the case of claims made against Lessor) litigated and/or reduced to judgment. In case any action or proceeding be brought against Lessor by reason of any of the foregoing matters, Lessee, upon notice from Lessor, shall defend the same at Lessee's expense by counsel reasonably satisfactory to Lessor and Lessor shall cooperate with Lessee in such defense. Lessor need not have first paid any such claim in order to be so indemnified.

8.8 EXEMPTION OF LESSOR FROM LIABILITY. Lessor shall not be liable for injury or damage to the person or goods, wares, merchandise or other property of Lessee, Lessee's employees, contractors, invitees, customers, or any other person in or about the Premises, whether such damage or injury is caused by or results from fire, steam, electricity, gas, water or rain, or from the breakage, leakage, obstruction or other defects of pipes, fire sprinklers, wires, appliances, plumbing, air conditioning or lighting fixtures, or from any other cause, whether said injury or damage results from conditions arising upon the Premises or upon other portions of the Building of which the Premises are a part, from other sources or places, and regardless of whether the cause of such damage or injury or the means of repairing the same is accessible or not. Lessor shall not be liable for any damages arising from any act or neglect of any other lessee of Lessor nor from the failure by Lessor to enforce the provisions of any other lease in the Industrial Center. Notwithstanding Lessor's negligence or breach of this Lease, Lessor shall under no circumstances be liable for injury to Lessee's business or for any loss of income or profit therefrom.

## 9. DAMAGE OR DESTRUCTION.

### 9.1 DEFINITIONS.

(a) "PREMISES PARTIAL DAMAGE" shall mean damage or destruction to the Premises, other than Lessee-Owned Alterations and Utility Installations, the repair cost of which damage or destruction is less than fifty percent (50%) of the then Replacement Cost (as defined in Paragraph 9.1(d)) of the Premises (excluding Lessee-Owned Alterations and Utility Installations and Trade Fixtures) immediately prior to such damage or destruction.

(b) "PREMISES TOTAL DESTRUCTION" shall mean damage or destruction to the Premises, other than Lessee-Owned Alterations and Utility Installations, the repair cost of which damage or destruction is fifty percent (50%) or more of the then Replacement Cost of the Premises (excluding Lessee-Owned Alterations and Utility Installations and Trade Fixtures) immediately prior to such damage or destruction. In addition, damage or destruction to the Building, other than Lessee-Owned Alterations and Utility Installations and Trade Fixtures of any lessees of the Building, the cost of which damage or destruction is fifty percent (50%) or more of the then Replacement Cost (excluding Lessee-Owned Alterations and Utility Installations and Trade Fixtures of any lessees of the Building) of the Building shall, at the option of Lessor, be deemed to be Premises Total Destruction.

(c) "INSURED LOSS" shall mean damage or destruction to the Premises, other than Lessee-Owned Alterations and Utility Installations and Trade Fixtures, which was caused by an event required to be covered by the insurance described in Paragraph 8.3(a) irrespective of any deductible amounts or coverage limits involved.

(d) "REPLACEMENT COST" shall mean the cost to repair or rebuild the improvements owned by Lessor at the time of the occurrence to their condition existing immediately prior thereto, including demolition, debris removal and upgrading required by the operation of applicable building codes, ordinances or laws, and without deduction for depreciation.

(e) "HAZARDOUS SUBSTANCE CONDITION" shall mean the occurrence or discovery of a condition involving the presence of, or a contamination by, a Hazardous Substance as defined in Paragraph 6.2(a), in, on, or under the Premises.

9.2 PREMISES PARTIAL DAMAGE -- INSURED LOSS. If Premises Partial Damage that is an Insured Loss occurs, then Lessor shall, at Lessor's expense, repair such damage (but not Lessee's Trade Fixtures or Lessee-Owned Alterations and

Utility Installations) as soon as reasonably possible and this Lease shall continue in full force and effect. In the event, however, that there is a shortage of insurance proceeds and such shortage is due to the fact that, by reason of the unique nature of the improvements in the Premises, full replacement cost insurance coverage was not commercially reasonable and available, Lessor shall have no obligation to pay for the shortage in insurance proceeds or to fully restore the unique aspects of the Premises unless Lessee provides Lessor with the funds to cover same, or adequate assurance thereof, within ten (10) days following receipt of written notice of such shortage and request therefor. If Lessor receives said funds or adequate assurance thereof within said ten (10) day period, Lessor shall complete them as soon as reasonably possible and this Lease shall remain in full force and effect. If Lessor does not receive such funds or assurance within said period, Lessor may nevertheless elect by written notice to Lessee within ten (10) days thereafter to make such restoration and repair as is commercially reasonable with Lessor paying any shortage in proceeds, in which case this Lease shall remain in full force and effect. If Lessor does not receive such funds or assurance within such ten (10) day period, and if Lessor does not so elect to restore and repair, then this Lease shall terminate sixty (60) days following the occurrence of the damage or destruction. Unless otherwise agreed, Lessee shall in no event have any right to reimbursement from Lessor for any funds contributed by Lessee to repair any such damage or destruction. Premises Partial Damage due to flood or earthquake shall be subject to Paragraph 9.3 rather than Paragraph 9.2, notwithstanding that there may be some insurance coverage, but the net proceeds of any such insurance shall be made available for the repairs if made by either Party.

9.3 PARTIAL DAMAGE -- UNINSURED LOSS. If Premises Partial Damage that is not an Insured Loss occurs, unless caused by a negligent or willful act of Lessee (in which event Lessee shall make the repairs at Lessee's expense and this Lease shall continue in full force and effect), Lessor may, at Lessor's option, either (i) repair such damage as soon as reasonably possible at Lessor's expense, in which event this Lease shall continue in full force and effect, or (ii) give written notice to Lessee within thirty (30) days after receipt by Lessor of knowledge of the occurrence of such damage of Lessor's desire to terminate this Lease as of the date sixty (60) days following the date of such notice. In the event Lessor elects to give such notice of Lessor's intention to terminate this Lease, Lessee shall have the right within ten (10) days after the receipt of such notice to give written notice to Lessor of Lessee's commitment to pay for the repair of such damage totally at Lessee's expense and without reimbursement from Lessor. Lessee shall provide Lessor with the required funds or satisfactory assurance thereof within thirty (30) days following such commitment from Lessee. In such event this Lease shall continue in full force and effect, and Lessor shall proceed to make such repairs as soon as reasonably possible after the required funds are available. If Lessee does not give such notice and provide the funds or assurance thereof within the times specified above, this Lease shall terminate as of the date specified in Lessor's notice of termination.

9.4 TOTAL DESTRUCTION. Notwithstanding any other provision hereof, if Premises Total Destruction occurs (including any destruction required by any authorized public authority), this Lease shall terminate sixty (60) days following the date of such Premises Total Destruction, whether or not the damage or destruction is an Insured Loss or was caused by a negligent or willful act of Lessee. In the event, however, that the damage or destruction was caused by Lessee, Lessor shall have the right to recover Lessor's damages from Lessee except as released and waived in Paragraph 9.7.

9.5 DAMAGE NEAR END OF TERM. If at any time during the last six (6) months of the term of this Lease there is damage for which the cost to repair exceeds one month's Base Rent, whether or not an Insured Loss, Lessor may, at Lessor's option, terminate this Lease effective sixty (60) days following the date of occurrence of such damage by giving written notice to Lessee of Lessor's election to do so within thirty (30) days after the date of occurrence of such damage. Provided, however, if Lessee at that time has an exercisable option to extend this Lease or to purchase the Premises, then Lessee may preserve this Lease by (a) exercising such option, and (b) providing Lessor with any shortage in insurance proceeds (or adequate assurance thereof) needed to make the repairs

on or before the earlier of (i) the date which is ten (10) days after Lessee's receipt of Lessor's written notice purporting to terminate this Lease, or (ii) the day prior to the date upon which such option expires. If Lessee duly exercises such option during such period and provides Lessor with funds (or adequate assurance thereof) to cover any shortage in insurance proceeds, Lessor shall, at Lessor's expense, repair such damage as soon as reasonably possible and this Lease shall continue in full force and effect. If Lessee fails to exercise such option and provide such funds or assurance during such period, then this Lease shall terminate as of the date set forth in the first sentence of this Paragraph 9.5.

#### 9.6 ABATEMENT OF RENT; LESSEE'S REMEDIES.

(a) In the event of (i) Premises Partial Damage or (ii) Hazardous Substance Condition for which Lessee is not legally responsible, the Base Rent, Common Area Operating Expenses and other charges, if any, payable by Lessee hereunder for the period during which such damage or condition, its repair, remediation or restoration continues, shall be abated in proportion to the degree to which Lessee's use of the Premises is impaired, but not in excess of proceeds from insurance required to be carried under Paragraph 8.3(b). Except for abatement of Base Rent, Common Area Operating Expenses and other charges, if any, as aforesaid, all other obligations of Lessee hereunder shall be performed by Lessee, and Lessee shall have no claim against Lessor for any damage suffered by reason of any such damage, destruction, repair, remediation or restoration.

(b) If Lessor shall be obligated to repair or restore the Premises under the provisions of this Paragraph 9 and shall not commence, in a substantial and meaningful way, the repair or restoration of the Premises within ninety (90) days after such obligation shall accrue, Lessee may, at any time prior to the commencement of such repair or restoration, give written notice to Lessor and to any Lenders of which Lessee has actual notice of Lessee's election to terminate this Lease on a date not less than sixty (60) days following the giving of such notice. If Lessee gives such notice to Lessor and such Lenders and such repair or restoration is not commenced within thirty (30) days after receipt of such notice, this Lease shall terminate as of the date specified in said notice. If Lessor or a Lender commences the repair or restoration of the Premises within thirty (30) days after the receipt of such notice, this Lease shall continue in full force and effect. "COMMENCE" as used in this Paragraph 9.6 shall mean either the unconditional authorization of the preparation of the required plans, or the beginning of the actual work on the Premises, whichever occurs first.

9.7 HAZARDOUS SUBSTANCE CONDITIONS. If a Hazardous Substance Condition occurs, unless Lessee is legally responsible therefor (in which case Lessee shall make the investigation and remediation thereof required by Applicable Requirements and this Lease shall continue in full force and effect, but subject

to Lessor's rights under Paragraph 6.2(c) and Paragraph 13), Lessor may, at Lessor's option, either (i) investigate and remediate such Hazardous Substance Condition, if required, as soon as reasonably possible at Lessor's expense, in which event this Lease shall continue in full force and effect, or (ii) if the estimated cost to investigate and remediate such condition exceeds twelve (12) times the then monthly Base Rent or \$100,000, whichever is greater, give written notice to Lessee within thirty (30) days after receipt by Lessor of knowledge of the occurrence of such Hazardous Substance Condition of Lessor's desire to terminate this Lease as of the date sixty (60) days following the date of such notice. In the event Lessor elects to give such notice of Lessor's intention to terminate this Lease, Lessee shall have the right within ten (10) days after the receipt of such notice to give written notice to Lessor of Lessee's commitment to pay for the excess costs of (a) investigation and remediation of such Hazardous Substance Condition to the extent required by Applicable Requirements, over (b) an amount equal to twelve (12) times the then monthly Base Rent or \$100,000, whichever is greater. Lessee shall provide Lessor with the funds

required of Lessee or satisfactory assurance thereof within thirty (30) days following said commitment by Lessee. In such event this Lease shall continue in full force and effect, and Lessor shall proceed to make such investigation and remediation as soon as reasonably possible after the required funds are available. If Lessee does not give such notice and provide the required funds or assurance thereof within the time period specified above, this Lease shall terminate as of the date specified in Lessor's notice of termination.

9.8 TERMINATION - ADVANCE PAYMENTS. Upon termination of this Lease pursuant to this Paragraph 9, Lessor shall return to Lessee any advance payment made by Lessee to Lessor and so much of Lessee's Security Deposit as has not been, or is not then required to be, used by Lessor under the terms of this Lease.

9.9 WAIVER OF STATUTES. Lessor and Lessee agree that the terms of this Lease shall govern the effect of any damage to or destruction of the Premises and the Building with respect to the termination of this Lease and hereby waive the provisions of any present or future statute to the extent it is inconsistent herewith.

#### 10. REAL PROPERTY TAXES.

10.1 PAYMENT OF TAXES. Lessor shall pay the Real Property Taxes, as defined in Paragraph 10.2, applicable to the Industrial Center, and except as otherwise provided in Paragraph 10.3, any such amounts shall be included in the calculation of Common Area Operating Expenses in accordance with the provisions of Paragraph 4.2.

10.2 REAL PROPERTY TAX DEFINITION. As used herein, the term "REAL PROPERTY TAXES" shall include any form of real estate tax or assessment, general, special, ordinary or extraordinary, and any license fee, commercial rental tax, improvement bond or bonds, levy or tax (other than inheritance, personal income or estate taxes) imposed upon the Industrial Center by any authority having the direct or indirect power to tax, including any city, state or federal government, or any school, agricultural, sanitary, fire, street, drainage, or other improvement district thereof, levied against any legal or equitable interest of Lessor in the Industrial Center or any portion thereof, Lessor's right to rent or other income therefrom, and/or Lessor's business of leasing the Premises. The term "REAL PROPERTY TAXES" shall also include any tax, fee, levy, assessment or charge, or any increase therein, imposed by reason of events occurring, or changes in Applicable Law taking effect, during the term of this Lease, including, but not limited to, a change in the ownership of the Industrial Center or in the improvements thereon, the execution of this Lease, or any modification, amendment or transfer thereof, and whether or not contemplated by the Parties. In calculating Real Property Taxes for any calendar year, the Real Property Taxes for any real estate tax year shall be included in the calculation of Real Property Taxes for such calendar year based upon the number of days which such calendar year and tax year have in common.

10.3 ADDITIONAL IMPROVEMENTS. Common Area Operating Expenses shall not include Real Property Taxes specified in the tax assessor's records and work sheets as being caused by additional improvements placed upon the Industrial Center by other lessees or by Lessor for the exclusive enjoyment of such other lessees. Notwithstanding Paragraph 10.1 hereof, Lessee shall, however, pay to Lessor at the time Common Area Operating Expenses are payable under Paragraph 4.2, the entirety of any increase in Real Property Taxes if assessed solely by reason of Alterations, Trade Fixtures or Utility Installations placed upon the Premises by Lessee or at Lessee's request.

10.4 JOINT ASSESSMENT. If the Building is not separately assessed, Real Property Taxes allocated to the Building shall be an equitable proportion of the Real Property Taxes for all of the land and improvements included within the tax parcel assessed, such proportion to be determined by Lessor from the respective valuations assigned in the assessor's work sheets or such other information as may be reasonably available. Lessor's reasonable determination thereof, in good faith, shall be conclusive.

10.5 LESSEE'S PROPERTY TAXES. Lessee shall pay prior to delinquency all taxes assessed against and levied upon Lessee-Owned Alterations and Utility

Installations, Trade Fixtures, furnishings, equipment and all personal property of Lessee contained in the Premises or stored within the Industrial Center. When possible, Lessee shall cause its Lessee-Owned Alterations and Utility Installations, Trade Fixtures, furnishings, equipment and all other personal property to be assessed and billed separately from the real property of Lessor. If any of Lessee's said property shall be assessed with Lessor's real property, Lessee shall pay Lessor the taxes attributable to Lessee's property within ten (10) days after receipt of a written statement setting forth the taxes applicable to Lessee's property.

11. UTILITIES. Lessee shall pay directly for all utilities and services supplied to the Premises, including, but not limited to, electricity, telephone, security, gas and cleaning of the Premises, together with any taxes thereon. If any such utilities or services are not separately metered to the Premises or separately billed to the Premises, Lessee shall pay to Lessor a reasonable proportion to be determined by Lessor of all such charges jointly metered or billed with other premises in the Building, in the manner and within the time periods set forth in Paragraph 4.2(d).

12. ASSIGNMENT AND SUBLETTING.

12.1 LESSOR'S CONSENT REQUIRED.

(a) Lessee shall not voluntarily or by operation of law assign, transfer, mortgage or otherwise transfer or encumber (collectively, "assign") or sublet all or any part of Lessee's interest in this Lease or in the Premises without Lessor's prior written consent given under and subject to the terms of Paragraph 36.

(b) A change in the control of Lessee shall constitute an assignment requiring Lessor's consent. The transfer, on a cumulative basis, of twenty-five percent (25%) or more of the voting control of Lessee shall constitute a change in control for this purpose.

(c) The involvement of Lessee or its assets in any transaction, or series of transactions (by way of merger, sale, acquisition, financing, refinancing, transfer, leveraged buy-out or otherwise), whether or not a formal assignment or hypothecation of this Lease or Lessee's assets occurs, which results or will result in a reduction of the Net Worth of Lessee, as hereinafter defined, by an amount equal to or greater than twenty-five percent (25%) of such Net Worth of Lessee as it was represented to Lessor at the time of full execution and delivery of this Lease or at the time of the most recent assignment to which Lessor has consented, or as it exists immediately prior to said transaction or transactions constituting such reduction, at whichever time said Net Worth of Lessee was or is greater, shall be considered an assignment of this Lease by Lessee to which Lessor may reasonably withhold its consent. "NET WORTH OF LESSEE" for purposes of this Lease shall be the net worth of Lessee (excluding any Guarantors) established under generally accepted accounting principles consistently applied.

(d) An assignment or subletting of Lessee's interest in this Lease without Lessor's specific prior written consent shall, at Lessor's option, be a Default curable after notice per Paragraph 13.1, or a non-curable Breach without the necessity of any notice and grace period. If Lessor elects to treat such unconsented to assignment or subletting as a non-curable Breach, Lessor shall have the right to either: (i) terminate this Lease, or (ii) upon thirty (30) days' written notice ("LESSOR'S NOTICE"), increase the monthly Base Rent for the Premises to the greater of the then fair market rental value of the Premises, as reasonably determined by Lessor, or one hundred ten percent (110%) of the Base Rent then in effect. Pending determination of the new fair market rental value, if disputed by Lessee, Lessee shall pay the amount set forth in Lessor's Notice, with any overpayment credited against the next installment(s) of Base Rent coming due, and any underpayment for the period retroactively to the effective date of the adjustment being due and payable immediately upon the determination thereof. Further, in the event of such Breach and rental adjustment, (i) the purchase price of any option to purchase the Premises held by Lessee shall be subject to similar adjustment to the then fair market value as reasonably determined by Lessor (without the Lease being considered an encumbrance or any



deduction for depreciation or obsolescence, and considering the Premises at its highest and best use and in good condition) or one hundred ten percent (110%) of the price previously in effect, (ii) any index-oriented rental or price adjustment formulas contained in this Lease shall be adjusted to require that the base index be determined with reference to the index applicable to the time of such adjustment, and (iii) any fixed rental adjustments scheduled during the remainder of the Lease term shall be increased in the same ratio as the new rental bears to the Base Rent in effect immediately prior the adjustment specified in Lessor's Notice.

(e) Lessee's remedy for any breach of this Paragraph 12.1 by Lessor shall be limited to compensatory damages and/or injunctive relief.

#### 12.2 TERMS AND CONDITIONS APPLICABLE TO ASSIGNMENT AND SUBLETTING.

(a) Regardless of Lessor's consent, any assignment or subletting shall not (i) be effective without the express written assumption by such assignee or sublessee of the obligations of Lessee under this Lease, (ii) release Lessee of any obligations hereunder, nor (iii) alter the primary liability of Lessee for the payment of Base Rent and other sums due Lessor hereunder or for the performance of any other obligations to be performed by Lessee under this Lease.

(b) Lessor may accept any rent or performance of Lessee's obligations from any person other than Lessee pending approval or disapproval of an assignment. Neither a delay in the approval or disapproval of such assignment nor the acceptance of any rent for performance shall constitute a waiver or estoppel of Lessor's right to exercise its remedies for the Default or Breach by Lessee of any of the terms, covenants or conditions of this Lease.

(c) The consent of Lessor to any assignment or subletting shall not constitute a consent to any subsequent assignment or subletting by Lessee or to any subsequent or successive assignment or subletting by the assignee or sublessee. However, Lessor may consent to subsequent sublettings and assignments of the sublease or any amendments or modifications thereto without notifying Lessee or anyone else liable under this Lease or the sublease and without obtaining their consent, and such action shall not relieve such persons from liability under this Lease or the sublease.

(d) In the event of any Default or Breach of Lessee's obligation under this Lease, Lessor may proceed directly against Lessee, any Guarantors or anyone else responsible for the performance of the Lessee's obligations under this Lease, including any sublessee, without first exhausting Lessor's remedies against any other person or entity responsible therefor to Lessor, or any security held by Lessor.

(e) Each request for consent to an assignment or subletting shall be in writing, accompanied by information relevant to Lessor's determination as to the financial and operational responsibility and appropriateness of the proposed assignee or sublessee, including, but not limited to, the intended use and/or required modification of the Premises, if any, together with a non-refundable deposit of \$1,000 or ten percent (10%) of the monthly Base Rent applicable to the portion of the Premises which is the subject of the proposed assignment or sublease, whichever is greater, as reasonable consideration for Lessor's considering and processing the request for consent. Lessee agrees to provide Lessor with such other or additional information and/or documentation as may be reasonably requested by Lessor.

(f) Any assignee of, or sublessee under, this Lease shall, by reason of accepting such assignment or entering into such sublease, be deemed, for the benefit of Lessor, to have assumed and agreed to conform and comply with each and every term, covenant, condition and obligation herein to be observed or performed by Lessee during the term of said assignment or sublease, other than such obligations as are contrary to or inconsistent with provisions of an assignment or sublease to which Lessor has specifically consented in writing.

(g) The occurrence of a transaction described in Paragraph 12.2(c) shall give Lessor the right (but not the obligation) to require that the Security Deposit be increased by an amount equal to six (6) times the then monthly Base Rent, and Lessor may make the actual receipt by Lessor of the Security Deposit increase a condition to Lessor's consent to such transaction.

(h) Lessor, as a condition to giving its consent to any assignment or subletting, may require that the amount and adjustment schedule of the rent payable under this Lease be adjusted to what is then the market value and/or adjustment schedule for property similar to the Premises as then constituted, as determined by Lessor.

12.3 ADDITIONAL TERMS AND CONDITIONS APPLICABLE TO SUBLETTING. The following terms and conditions shall apply to any subletting by Lessee of all or any part of the Premises and shall be deemed included in all subleases under this Lease whether or not expressly incorporated therein:

(a) Lessee hereby assigns and transfers to Lessor all of Lessee's interest in all rentals and income arising from any sublease of all or a portion of the Premises heretofore or hereafter made by Lessee, and Lessor may collect such rent and income and apply same toward Lessee's obligations under this Lease; provided, however, that until a Breach (as defined in Paragraph 13.1) shall occur in the performance of Lessee's obligations under this Lease, Lessee may, except as otherwise provided in this Lease, receive, collect and enjoy the rents accruing under such sublease. Lessor shall not, by reason of the foregoing provision or any other assignment of such sublease to Lessor, nor by reason of the collection of the rents from a sublessee, be deemed liable to the sublessee for any failure of Lessee to perform and comply with any of Lessee's obligations to such sublessee under such Sublease. Lessee hereby irrevocably authorizes and directs any such sublessee, upon receipt of a written notice from Lessor stating that a Breach exists in the performance of Lessee's obligations under this Lease, to pay to Lessor the rents and other charges due and to become due under the sublease. Sublessee shall rely upon any such statement and request from Lessor and shall pay such rents and other charges to Lessor without any obligation or right to inquire as to whether such Breach exists and notwithstanding any notice from or claim from Lessee to the contrary. Lessee shall have no right or claim against such sublessee, or, until the Breach has been cured, against Lessor, for any such rents and other charges so paid by said sublessee to Lessor.

(b) In the event of a Breach by Lessee in the performance of its obligations under this Lease, Lessor, at its option and without any obligation to do so, may require any sublessee to attorn to Lessor, in which event Lessor shall undertake the obligations of the sublessor under such sublease from the time of the exercise of said option to the expiration of such sublease; provided, however, Lessor shall not be liable for any prepaid rents or security deposit paid by such sublessee to such sublessor or for any other prior defaults or breaches of such sublessor under such sublease.

(c) Any matter or thing requiring the consent of the sublessor under a sublease shall also require the consent of Lessor herein.

(d) No sublessee under a sublease approved by Lessor shall further assign or sublet all or any part of the Premises without Lessor's prior written consent.

(e) Lessor shall deliver a copy of any notice of Default or Breach by Lessee to the sublessee, who shall have the right to cure the Default of Lessee within the grace period, if any, specified in such notice. The sublessee shall have a right of reimbursement and offset from and against Lessee for any such Defaults cured by the sublessee. See Paragraph 55.

### 13. DEFAULT; BREACH; REMEDIES.

13.1 DEFAULT; BREACH. Lessor and Lessee agree that if an attorney is

consulted by Lessor in connection with a Lessee Default or Breach (as hereinafter defined), \$350.00 is a reasonable minimum sum per such occurrence for legal services and costs in the preparation and service of a notice of Default, and that Lessor may include the cost of such services and costs in said notice as rent due and payable to cure said default. A "DEFAULT" by Lessee is defined as a failure by Lessee to observe, comply with or perform any of the terms, covenants, conditions or rules applicable to Lessee under this Lease. A "BREACH" by Lessee is defined as the occurrence of any one or more of the following Defaults, and, where a grace period for cure after notice is specified herein, the failure by Lessee to cure such Default prior to the expiration of the applicable grace period, and shall entitle Lessor to pursue the remedies set forth in Paragraphs 13.2 and/or 13.3:

(a) The vacating of the Premises without the intention to reoccupy same, or the abandonment of the Premises.

(b) Except as expressly otherwise provided in this Lease, the failure by Lessee to make any payment of Base Rent, Lessee's Share of Common Area Operating Expenses, or any other monetary payment required to be made by Lessee hereunder as and when due, the failure by Lessee to provide Lessor with reasonable evidence of insurance or surety bond required under this Lease, or the failure of Lessee to fulfill any obligation under this Lease which endangers or threatens life or property, where such failure continues for a period of three (3) days following written notice thereof by or on behalf of Lessor to Lessee.

(c) Except as expressly otherwise provided in this Lease, the failure by Lessee to provide Lessor with reasonable written evidence (in duly executed original form, if applicable) of (i) compliance with Applicable Requirements per Paragraph 6.3, (ii) the inspection, maintenance and service contracts required under Paragraph 7.1(b), (iii) the rescission of an unauthorized assignment or subletting per Paragraph 12.1, (iv) a Tenancy Statement per Paragraphs 16 or 37, (v) the subordination or non-subordination of this Lease per Paragraph 30, (vi) the guaranty of the performance of Lessee's obligations under this Lease if required under Paragraphs 1.11 and 37, (vii) the execution of any document requested under Paragraph 42 (easements), or (viii) any other documentation or information which Lessor may reasonably require of Lessee under the terms of this Lease, where any such failure continues for a period of ten (10) days following written notice by or on behalf of Lessor to Lessee.

(d) A Default by Lessee as to the terms, covenants, conditions or provisions of this Lease, or of the rules adopted under Paragraph 40 hereof that are to be observed, complied with or performed by Lessee, other than those described in Subparagraphs 13.1(a), (b) or (c), above, where such Default continues for a period of thirty (30) days after written notice thereof by or on behalf of Lessor to Lessee; provided, however, that if the nature of Lessee's Default is such that more than thirty (30) days are reasonably required for its cure, then it shall not be deemed to be a Breach of this Lease by Lessee if Lessee commences such cure within said thirty (30) day period and thereafter diligently prosecutes such cure to completion.

(e) The occurrence of any of the following events: (i) the making by Lessee of any general arrangement or assignment for the benefit of creditors; (ii) Lessee's becoming a "debtor" as defined in 11 U.S. Code Section 101 or any successor statute thereto (unless, in the case of a petition filed against Lessee, the same is dismissed within sixty (60) days); (iii) the appointment of a trustee or receiver to take possession of substantially all of Lessee's assets located at the Premises or of Lessee's interest in this Lease, where possession is not restored to Lessee within thirty (30) days; or (iv) the attachment, execution or other judicial seizure of substantially all of Lessee's assets located at the Premises or of Lessee's interest in this Lease, where such seizure is not discharged within thirty (30) days; provided, however, in the event that any provision of this Subparagraph 13.1(e) is contrary to any applicable law, such provision shall be of no force or effect, and shall not affect the validity of the remaining provisions.

(f) The discovery by Lessor that any financial statement of Lessee

or of any Guarantor, given to Lessor by Lessee or any Guarantor, was materially false.

13.2 REMEDIES. If Lessee fails to perform any affirmative duty or obligation of Lessee under this Lease, within ten (10) days after written notice to Lessee (or in case of an emergency, without notice), Lessor may at its option (but without obligation to do so), perform such duty or obligation on Lessee's behalf, including, but not limited to, the obtaining of reasonably required bonds, insurance policies, or governmental licenses, permits or approvals. The costs and expenses of any such performance by Lessor shall be due and payable by Lessee to Lessor upon invoice therefor. If any check given to Lessor by Lessee shall not be honored by the bank upon which it is drawn, Lessor, at its own option, may require all future payments to be made under this Lease by Lessee to be made only by cashier's check. In the event of a Breach of this Lease by Lessee (as defined in Paragraph 13.1), with or without further notice or demand, and without limiting Lessor in the exercise of any right or remedy which Lessor may have by reason of such Breach, Lessor may:

(a) Terminate Lessee's right to possession of the Premises by any lawful means, in which case this Lease and the term hereof shall terminate and Lessee shall immediately surrender possession of the Premises to Lessor. In such event Lessor shall be entitled to recover from Lessee: (i) the worth at the time of the award of the unpaid rent which had been earned at the time of termination; (ii) the worth at the time of award of the amount by which the unpaid rent which would have been earned after termination until the time of award exceeds the amount of such rental loss that the Lessee proves could have been reasonably avoided; (iii) the worth at the time of award of the amount by which the unpaid rent for the balance of the term after the time of award exceeds the amount of such rental loss that the Lessee proves could be reasonably avoided; and (iv) any other amount necessary to compensate Lessor for all the detriment proximately caused by the Lessee's failure to perform its obligations under this Lease or which in the ordinary course of things would be likely to result therefrom, including, but not limited to, the cost of recovering possession of the Premises, expenses of reletting, including necessary renovation and alteration of the Premises, reasonable attorneys' fees, and that portion of any leasing commission paid by Lessor in connection with this Lease applicable to the unexpired term of this Lease. The worth at the time of award of the amount referred to in provision (iii) of the immediately preceding sentence shall be computed by discounting such amount at the discount rate of the Federal Reserve Bank of San Francisco or the Federal Reserve Bank District in which the Premises are located at the time of award plus one percent (1%). Efforts by Lessor to mitigate damages caused by Lessee's Default or Breach of this Lease shall not waive Lessor's right to recover damages under this Paragraph 13.2. If termination of this Lease is obtained through the provisional remedy of unlawful detainer, Lessor shall have the right to recover in such proceeding the unpaid rent and damages as are recoverable therein, or Lessor may reserve the right to recover all or any part thereof in a separate suit for such rent and/or damages. If a notice and grace period required under Subparagraphs 13.1(b), (c) or (d) was not previously given, a notice to pay rent or quit, or to perform or quit, as the case may be, given to Lessee under any statute authorizing the forfeiture of leases for unlawful detainer shall also constitute the applicable notice for grace period purposes required by Subparagraph 13.1(b), (c) or (d). In such case, the applicable grace period under the unlawful detainer statute shall run concurrently after the one such statutory notice, and the failure of Lessee to cure the Default within the greater of the two (2) such grace periods shall constitute both an unlawful detainer and a Breach of this Lease entitling Lessor to the remedies provided for in this Lease and/or by said statute.

(b) Continue the Lease and Lessee's right to possession in effect (in California under California Civil Code Section 1951.4) after Lessee's Breach and recover the rent as it becomes due, provided Lessee has the right to sublet or assign, subject only to reasonable limitations. Lessor and Lessee agree that the limitations on assignment and subletting in this Lease are reasonable. Acts of maintenance or preservation, efforts to relet the Premises, or the appointment of a receiver to protect the Lessor's interest under this Lease, shall not constitute a termination of the Lessee's right to possession.

(c) Pursue any other remedy now or hereafter available to Lessor under the laws or judicial decisions of the state wherein the Premises are located.

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(d) The expiration or termination of this Lease and/or the termination of Lessee's right to possession shall not relieve Lessee from liability under any indemnity provisions of this Lease as to matters occurring or accruing during the term hereof or by reason of Lessee's occupancy of the Premises.

13.4 LATE CHARGES. Lessee hereby acknowledges that late payment by Lessee to Lessor of rent and other sums due hereunder will cause Lessor to incur costs not contemplated by this Lease, the exact amount of which will be extremely difficult to ascertain. Such costs include, but are not limited to, processing and accounting charges, and late charges which may be imposed upon Lessor by the terms of any ground lease, mortgage or deed of trust covering the Premises. Accordingly, if any installment of rent or other sum due from Lessee shall not be received by Lessor or Lessor's designee within ten (10) days after such amount shall be due, then, without any requirement for notice to Lessee, Lessee shall pay to Lessor a late charge equal to six percent (6%) of such overdue amount. The Parties hereby agree that such late charge represents a fair and reasonable estimate of the costs Lessor will incur by reason of late payment by Lessee. Acceptance of such late charge by Lessor shall in no event constitute a waiver of Lessee's Default or Breach with respect to such overdue amount, nor prevent Lessor from exercising any of the other rights and remedies granted hereunder. In the event that a late charge is payable hereunder, whether or not collected, for three (3) consecutive installments of Base Rent, then notwithstanding Paragraph 4.1 or any other provision of this Lease to the contrary, Base Rent shall, at Lessor's option, become due and payable quarterly in advance.

13.5 BREACH BY LESSOR. Lessor shall not be deemed in breach of this Lease unless Lessor fails, except in cases of emergency, within a reasonable time to perform an obligation required to be performed by Lessor. For purposes of this Paragraph 13.5, a reasonable time shall in no event be less than thirty (30) days after receipt by Lessor, and by any Lender(s) whose name and address shall have been furnished to Lessee in writing for such purpose, of written notice specifying wherein such obligation of Lessor has not been performed; provided, however, that if the nature of Lessor's obligation is such that more than thirty (30) days after such notice are reasonably required for its performance, then Lessor shall not be in breach of this Lease if performance is commenced within such thirty (30) day period and thereafter diligently pursued to completion.

14. CONDEMNATION. If the Premises or any portion thereof are taken under the power of eminent domain or sold under the threat of the exercise of said power (all of which are herein called "condemnation"), this Lease shall terminate as to the part so taken as of the date the condemning authority takes title or possession, whichever first occurs. If more than ten percent (10%) of the floor area of the Premises, or more than twenty-five percent (25%) of the portion of the Common Areas designated for Lessee's parking, is taken by condemnation, Lessee may, at Lessee's option, to be exercised in writing within ten (10) days after Lessor shall have given Lessee written notice of such taking (or in the absence of such notice, within ten (10) days after the condemning authority shall have taken possession) terminate this Lease as of the date the condemning authority takes such possession. If Lessee does not terminate this Lease in accordance with the foregoing, this Lease shall remain in full force and effect as to the portion of the Premises remaining, except that the Base Rent shall be reduced in the same proportion as the rentable floor area of the Premises taken bears to the total rentable floor area of the Premises. No reduction of Base Rent shall occur if the condemnation does not apply to any portion of the Premises. Any award for the taking of all or any part of the Premises under the power of eminent domain or any payment made under threat of the exercise of such power shall be the property of Lessor, whether such award shall be made as

compensation for diminution of value of the leasehold or for the taking of the fee, or as severance damages; provided, however, that Lessee shall be entitled to any compensation, separately awarded to Lessee for Lessee's relocation expenses and/or loss of Lessee's Trade Fixtures. In the event that this Lease is not terminated by reason of such condemnation, Lessor shall to the extent of its net severance damages received, over and above Lessee's share of the legal and other expenses incurred by Lessor in the condemnation matter, repair any damage to the Premises caused by such condemnation authority. Lessee shall be responsible for the payment of any amount in excess of such net severance damages required to complete such repair.

#### 16. TENANCY AND FINANCIAL STATEMENTS.

16.1 TENANCY STATEMENT. Each Party (as "RESPONDING PARTY") shall within ten (10) days after written notice from the other Party (the "REQUESTING PARTY") execute, acknowledge and deliver to the Requesting Party a statement in writing in a form similar to the then most current "TENANCY STATEMENT" form published by the American Industrial Real Estate Association, plus such additional information, confirmation and/or statements as may be reasonably requested by the Requesting Party.

16.2 FINANCIAL STATEMENT. If Lessor desires to finance, refinance, or sell the Premises or the Building, or any part thereof, Lessee and all Guarantors shall deliver to any potential lender or purchaser designated by Lessor such financial statements of Lessee and such Guarantors as may be reasonably required by such lender or purchaser, including, but not limited to, Lessee's financial statements for the past three (3) years. All such financial statements shall be received by Lessor and such lender or purchaser in confidence and shall be used only for the purposes herein set forth.

17. LESSOR'S LIABILITY. The term "LESSOR" as used herein shall mean the owner or owners at the time in question of the fee title to the Premises. In the event of a transfer of Lessor's title or interest in the Premises or in this Lease, Lessor shall deliver to the transferee or assignee (in cash or by credit) any unused Security Deposit held by Lessor at the time of such transfer or assignment. Except as provided in Paragraph 15.3, upon such transfer or assignment and delivery of the Security Deposit, as aforesaid, the prior Lessor shall be relieved of all liability with respect to the obligations and/or covenants under this Lease thereafter to be performed by the Lessor. Subject to the foregoing, the obligations and/or covenants in this Lease to be performed by the Lessor shall be binding only upon the Lessor as hereinabove defined.

18. SEVERABILITY. The invalidity of any provision of this Lease, as determined by a court of competent jurisdiction, shall in no way affect the validity of any other provision hereof.

19. INTEREST ON PAST-DUE OBLIGATIONS. Any monetary payment due Lessor hereunder, other than late charges, not received by Lessor within ten (10) days following the date on which it was due, shall bear interest from the date due at the prime rate of ten percent (10%) per annum in addition to the potential late charge provided for in Paragraph 13.4.

20. TIME OF ESSENCE. Time is of the essence with respect to the performance of all obligations to be performed or observed by the Parties under this Lease.

21. RENT DEFINED. All monetary obligations of Lessee to Lessor under the terms of this Lease are deemed to be rent.

22. NO PRIOR OR OTHER AGREEMENTS. This Lease contains all agreements between the Parties with respect to any matter mentioned herein, and no other prior or contemporaneous agreement or understanding shall be effective. Lessor and Lessee each represents and warrants to the Brokers that it has made, and is relying solely upon, its own investigation as to the nature, quality, character and financial responsibility of the other Party to this Lease and as to the nature, quality and character of the Premises. See Paragraph 56.

#### 23. NOTICES.

23.1 NOTICE REQUIREMENTS. All notices required or permitted by this Lease shall be in writing and may be delivered in person (by hand or by messenger or courier service) or may be sent by regular, certified or registered mail or U.S. Postal Service Express Mail, with postage prepaid, or by facsimile transmission during normal business hours, and shall be deemed sufficiently given if served in a manner specified in this Paragraph 23. The addresses noted adjacent to a Party's signature on this Lease shall be that Party's address for delivery or mailing of notice purposes. Either Party may by written notice to the other specify a different address for notice purposes, except that upon Lessee's taking possession of the Premises, the Premises shall constitute Lessee's address for the purpose of mailing or delivering notices to Lessee. A copy of all notices required or permitted to be given to Lessor hereunder shall be concurrently transmitted to such party or parties at such addresses as Lessor may from time to time hereafter designate by written notice to Lessee.

23.2 DATE OF NOTICE. Any notice sent by registered or certified mail, return receipt requested, shall be deemed given on the date of delivery shown on the receipt card, or if no delivery date is shown, the postmark thereon. If sent by regular mail, the notice shall be deemed given forty-eight (48) hours after the same is addressed as required herein and mailed with postage prepaid. Notices delivered by United States Express Mail or overnight courier that guarantees next day

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delivery shall be deemed given twenty-four (24) hours after delivery of the same to the United States Postal Service or courier. If any notice is transmitted by facsimile transmission or similar means, the same shall be deemed served or delivered upon telephone or facsimile confirmation of receipt of the transmission thereof, provided a copy is also delivered via delivery or mail. If notice is received on a Saturday or a Sunday or a legal holiday, it shall be deemed received on the next business day.

24. WAIVERS. No waiver by Lessor of the Default or Breach of any term, covenant or condition hereof by Lessee, shall be deemed a waiver of any other term, covenant or condition hereof, or of any subsequent Default or Breach by Lessee of the same or any other term, covenant or condition hereof. Lessor's consent to, or approval of, any such act shall not be deemed to render unnecessary the obtaining of Lessor's consent to, or approval of, any subsequent or similar act by Lessee, or be construed as the basis of an estoppel to enforce the provision or provisions of this Lease requiring such consent. Regardless of Lessor's knowledge of a Default or Breach at the time of accepting rent, the acceptance of rent by Lessor shall not be a waiver of any Default or Breach by Lessee of any provision hereof. Any payment given Lessor by Lessee may be accepted by Lessor on account of monies or damages due Lessor, notwithstanding any qualifying statements or conditions made by Lessee in connection therewith, which such statements and/or conditions shall be of no force or effect whatsoever unless specifically agreed to in writing by Lessor at or before the time of deposit of such payment.

25. RECORDING. Either Lessor or Lessee shall, upon request of the other, execute, acknowledge and deliver to the other a short form memorandum of this Lease for recording purposes. The Party requesting recordation shall be responsible for payment of any fees or taxes applicable thereto.

26. NO RIGHT TO HOLDOVER. Lessee has no right to retain possession of the Premises or any part thereof beyond the expiration or earlier termination of this Lease. In the event that Lessee holds over in violation of this Paragraph 26 then the Base Rent payable from and after the time of the expiration or earlier termination of this Lease shall be increased to two hundred percent (200%) of the Base Rent applicable during the month immediately preceding such expiration or earlier termination. Nothing contained herein shall be construed as a consent by Lessor to any holding over by Lessee.

27. CUMULATIVE REMEDIES. No remedy or election hereunder shall be deemed

exclusive but shall, wherever possible, be cumulative with all other remedies at law or in equity.

28. COVENANTS AND CONDITIONS. All provisions of this Lease to be observed or performed by Lessee are both covenants and conditions.

29. BINDING EFFECT; CHOICE OF LAW. This Lease shall be binding upon the Parties, their personal representatives, successors and assigns and be governed by the laws of the state in which the Premises are located. Any litigation between the Parties hereto concerning this Lease shall be initiated in the county in which the Premises are located.

30. SUBORDINATION; ATTORNMENT; NON-DISTURBANCE.

30.1 SUBORDINATION. This Lease and any Option granted hereby shall be subject and subordinate to any ground lease, mortgage, deed of trust, or other hypothecation or security device (collectively, "SECURITY DEVICE"), now or hereafter placed by Lessor upon the real property of which the Premises are a part, to any and all advances made on the security thereof, and to all renewals, modifications, consolidations, replacements and extensions thereof. Lessee agrees that the Lenders holding any such Security Device shall have no duty, liability or obligation to perform any of the obligations of Lessor under this Lease, but that in the event of Lessor's default with respect to any such obligation, Lessee will give any Lender whose name and address have been furnished Lessee in writing for such purpose notice of Lessor's default pursuant to Paragraph 13.5. If any Lender shall elect to have this Lease and/or any Option granted hereby superior to the lien of its Security Device and shall give written notice thereof to Lessee, this Lease and such Options shall be deemed prior to such Security Device, notwithstanding the relative dates of the documentation or recordation thereof.

30.2 ATTORNMENT. Subject to the non-disturbance provisions of Paragraph 30.3, Lessee agrees to attorn to a Lender or any other party who acquires ownership of the Premises by reason of a foreclosure of a Security Device, and that in the event of such foreclosure, such new owner shall not: (i) be liable for any act or omission of any prior lessor or with respect to events occurring prior to acquisition of ownership, (ii) be subject to any offsets or defenses which Lessee might have against any prior lessor, or (iii) be bound by prepayment of more than one (1) month's rent.

30.3 NON-DISTURBANCE. With respect to Security Devices entered into by Lessor after the execution of this Lease, Lessee's subordination of this Lease shall be subject to receiving assurance (a "non-disturbance agreement") from the Lender that Lessee's possession and this Lease, including any options to extend the term hereof, will not be disturbed so long as Lessee is not in Breach hereof and attorns to the record owner of the Premises.

30.4 SELF-EXECUTING. The agreements contained in this Paragraph 30 shall be effective without the execution of any further documents; provided, however, that upon written request from Lessor or a Lender in connection with a sale, financing or refinancing of Premises, Lessee and Lessor shall execute such further writings as may be reasonably required to separately document any such subordination or non-subordination, attornment and/or non-disturbance agreement as is provided for herein.

31. ATTORNEYS' FEES. If any Party or Broker brings an action or proceeding to enforce the terms hereof or declare rights hereunder, the Prevailing Party (as hereafter defined) in any such proceeding, action, or appeal thereon, shall be entitled to reasonable attorneys' fees. Such fees may be awarded in the same suit or recovered in a separate suit, whether or not such action or proceeding is pursued to decision or judgment. The term "PREVAILING PARTY" shall include, without limitation, a Party or Broker who substantially obtains or defeats the relief sought, as the case may be, whether by compromise, settlement, judgment, or the abandonment by the other Party or Broker of its claim or defense. The attorneys' fee award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all attorneys' fees reasonably incurred. Lessor shall be entitled to attorneys' fees, costs and expenses incurred in preparation and service of notices of Default and consultations in



connection therewith, whether or not a legal action is subsequently commenced in connection with such Default or resulting Breach. Broker(s) shall be intended third party beneficiaries of this Paragraph 31.

32. LESSOR'S ACCESS; SHOWING PREMISES; REPAIRS. Lessor and Lessor's agents shall have the right to enter the Premises at any time, in the case of an emergency, and otherwise at reasonable times for the purpose of showing the same to prospective purchasers, lenders, or lessees, and making such alterations, repairs, improvements or additions to the Premises or to the Building, as Lessor may reasonably deem necessary. Lessor may at any time place on or about the Premises or Building any ordinary "For Sale" signs and Lessor may at any time during the last one hundred eighty (180) days of the term hereof place on or about the Premises any ordinary "For Lease" signs. All such activities of Lessor shall be without abatement of Rent or liability to Lessee.

33. AUCTIONS. Lessee shall not conduct, nor permit to be conducted, either voluntarily or involuntarily, any auction upon the Premises without first having obtained Lessor's prior written consent. Notwithstanding anything to the contrary in this Lease, Lessor shall not be obligated to exercise any standard of reasonableness in determining whether to grant such consent.

34. SIGNS. Lessee shall not place any sign upon the exterior of the Premises or the Building, except that Lessee may, with Lessor's prior written consent, install (but not on the roof) such signs as are reasonably required to advertise Lessee's own business so long as such signs are in a location designated by Lessor and comply with Applicable Requirements and the signage criteria established for the Industrial Center by Lessor. The installation of any sign on the Premises by or for Lessee shall be subject to the provisions of Paragraph 7 (Maintenance, Repairs, Utility Installations, Trade Fixtures and Alterations). Unless otherwise expressly agreed herein, Lessor reserves all rights to the use of the roof of the Building, and the right to install advertising signs on the Building, including the roof, which do not unreasonably interfere with the conduct of Lessee's business; Lessor shall be entitled to all revenues from such advertising signs.

35. TERMINATION; MERGER. Unless specifically stated otherwise in writing by Lessor, the voluntary or other surrender of this Lease by Lessee, the mutual termination or cancellation hereof, or a termination hereof by Lessor for Breach by Lessee, shall automatically terminate any sublease or lesser estate in the Premises; provided, however, Lessor shall, in the event of any such surrender, termination or cancellation, have the option to continue any one or all of any existing subtenancies. Lessor's failure within ten (10) days following any such event to make a written election to the contrary by written notice to the holder of any such lesser interest, shall constitute Lessor's election to have such event constitute the termination of such interest.

36. CONSENTS.

(a) Except for Paragraph 33 hereof (Auctions) or as otherwise provided herein, wherever in this Lease the consent of a Party is required to an act by or for the other Party, such consent shall not be unreasonably withheld or delayed. Lessor's actual reasonable costs and expenses (including, but not limited to, architects', attorneys', engineers' and other consultants' fees) incurred in the consideration of, or response to, a request by Lessee for any Lessor consent pertaining to this Lease or the Premises, including, but not limited to, consents to an assignment, a subletting or the presence or use of a Hazardous Substance, shall be paid by Lessee to Lessor upon receipt of an invoice and supporting documentation therefor. In addition to the deposit described in Paragraph 12.2(e), Lessor may, as a condition to considering any such request by Lessee, require that Lessee deposit with Lessor an amount of money (in addition to the Security Deposit held under Paragraph 5) reasonably calculated by Lessor to represent the cost Lessor will incur in considering and responding to Lessee's request. Any unused portion of said deposit shall be refunded to Lessee without interest. Lessor's consent to any act, assignment of this Lease or subletting of the Premises by Lessee shall not constitute an acknowledgment that no Default or Breach by Lessee of this Lease exists, nor shall such consent be deemed a waiver of any then existing Default or Breach, except as may be otherwise specifically stated in writing by Lessor at the time

of such consent.

(b) All conditions to Lessor's consent authorized by this Lease are acknowledged by Lessee as being reasonable. The failure to specify herein any particular condition to Lessor's consent shall not preclude the impositions by Lessor at the time of consent of such further or other conditions as are then reasonable with reference to the particular matter for which consent is being given.

38. QUIET POSSESSION. Upon payment by Lessee of the Rent for the Premises and the performance of all of the covenants, conditions and provisions on Lessee's part to be observed and performed under this Lease, Lessee shall have quiet possession of the Premises for the entire term hereof subject to all of the provisions of this Lease.

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39. OPTIONS.

39.1 DEFINITION. As used in this Lease, the word "OPTION" has the following meaning: (a) the right to extend the term of this Lease or to renew this Lease.

39.2 OPTIONS PERSONAL TO ORIGINAL LESSEE. Each Option granted to Lessee in this Lease is personal to the original Lessee named in Paragraph 1.1 hereof, and cannot be voluntarily or involuntarily assigned or exercised by any person or entity other than said original Lessee while the original Lessee is in full and actual possession of the Premises and without the intention of thereafter assigning or subletting. The Options, if any, herein granted to Lessee are not assignable, either as a part of an assignment of this Lease or separately or apart therefrom, and no Option may be separated from this Lease in any manner, by reservation or otherwise.

39.3 MULTIPLE OPTIONS. In the event that Lessee has any multiple Options to extend or renew this Lease, a later option cannot be exercised unless the prior Options to extend or renew this Lease have been validly exercised.

39.4 EFFECT OF DEFAULT ON OPTIONS.

(a) Lessee shall have no right to exercise an Option, notwithstanding any provision in the grant of Option to the contrary: (i) during the period commencing with the giving of any notice of Default under Paragraph 13.1 and continuing until the noticed Default is cured, or (ii) during the period of time any monetary obligation due Lessor from Lessee is unpaid (without regard to whether notice thereof is given Lessee), or (iii) during the time Lessee is in Breach of this Lease, or (iv) in the event that Lessor has given to Lessee three (3) or more notices of separate Default under Paragraph 13.1 during the twelve (12) month period immediately preceding the exercise of the Option, whether or not the Defaults are cured.

(b) The period of time within which an Option may be exercised shall not be extended or enlarged by reason of Lessee's inability to exercise an Option because of the provisions of Paragraph 39.4(a).

(c) All rights of Lessee under the provisions of an Option shall terminate and be of no further force or effect, notwithstanding Lessee's due and timely exercise of the Option, if, after such exercise and during the term of this Lease, (i) Lessee fails to pay to Lessor a monetary obligation of Lessee for a period of thirty (30) days after such obligation becomes due (without any necessity of Lessor to give notice thereof to Lessee), or (ii) Lessor gives to Lessee three (3) or more notices of separate Defaults under Paragraph 13.1 during any twelve (12) month period, whether or not the Defaults are cured, or (iii) if Lessee commits a Breach of this Lease.

40. RULES AND REGULATIONS. Lessee agrees that it will abide by, and keep and observe all reasonable rules and regulations ("RULES AND REGULATIONS") which

Lessor may make from time to time for the management, safety, care, and cleanliness of the grounds, the parking and unloading of vehicles and the preservation of good order, as well as for the convenience of other occupants or tenants of the Building and the Industrial Center and their invitees.

41. SECURITY MEASURES. Lessee hereby acknowledges that the rental payable to Lessor hereunder does not include the cost of guard service or other security measures, and that Lessor shall have no obligation whatsoever to provide same. Lessee assumes all responsibility for the protection of the Premises, Lessee, its agents and invitees and their property from the acts of third parties.

42. RESERVATIONS. Lessor reserves the right, from time to time, to grant, without the consent or joinder of Lessee, such easements, rights of way, utility raceways, and dedications that Lessor deems necessary, and to cause the recordation of parcel maps and restrictions, so long as such easements, rights of way, utility raceways, dedications, maps and restrictions do not reasonably interfere with the use of the Premises by Lessee. Lessee agrees to sign any documents reasonably requested by Lessor to effectuate any such easement rights, dedication, map or restrictions.

43. PERFORMANCE UNDER PROTEST. If at any time a dispute shall arise as to any amount or sum of money to be paid by one Party to the other under the provisions hereof, the Party against whom the obligation to pay the money is asserted shall have the right to make payment "under protest" and such payment shall not be regarded as a voluntary payment and there shall survive the right on the part of said Party to institute suit for recovery of such sum. If it shall be adjudged that there was no legal obligation on the part of said Party to pay such sum or any part thereof, said Party shall be entitled to recover such sum or so much thereof as it was not legally required to pay under the provisions of this Lease.

44. AUTHORITY. If either Party hereto is a corporation, trust, or general or limited partnership, each individual executing this Lease on behalf of such entity represents and warrants that he or she is duly authorized to execute and deliver this Lease on its behalf. If Lessee is a corporation, trust or partnership, Lessee shall, within thirty (30) days after request by Lessor, deliver to Lessor evidence satisfactory to Lessor of such authority.

45. CONFLICT. Any conflict between the printed provisions of this Lease and the typewritten or handwritten provisions shall be controlled by the typewritten or handwritten provisions.

46. OFFER. Preparation of this Lease by either Lessor or Lessee or Lessor's agent or Lessee's agent and submission of same to Lessee or Lessor shall not be deemed an offer to lease. This Lease is not intended to be binding until executed and delivered by all Parties hereto.

47. AMENDMENTS. This Lease may be modified only in writing, signed by the Parties in interest at the time of the modification. The Parties shall amend this Lease from time to time to reflect any adjustments that are made to the Base Rent or other rent payable under this Lease. As long as they do not materially change Lessee's obligations hereunder, Lessee agrees to make such reasonable non-monetary modifications to this Lease as may be reasonably required by an institutional insurance company or pension plan Lender in connection with the obtaining of normal financing or refinancing of the property of which the Premises are a part.

48. MULTIPLE PARTIES. Except as otherwise expressly provided herein, if more than one person or entity is named herein as either Lessor or Lessee, the obligations of such multiple parties shall be the joint and several responsibility of all persons or entities named herein as such Lessor or Lessee.

PROVISION CONTAINED HEREIN, AND BY THE EXECUTION OF THIS LEASE SHOW THEIR INFORMED AND VOLUNTARY CONSENT THERETO. THE PARTIES HEREBY AGREE THAT, AT THE TIME THIS LEASE IS EXECUTED, THE TERMS OF THIS LEASE ARE COMMERCIALY REASONABLE AND EFFECTUATE THE INTENT AND PURPOSE OF LESSOR AND LESSEE WITH RESPECT TO THE PREMISES.

IF THIS LEASE HAS BEEN FILLED IN, IT HAS BEEN PREPARED FOR YOUR ATTORNEY'S REVIEW AND APPROVAL. FURTHER, EXPERTS SHOULD BE CONSULTED TO EVALUATE THE CONDITION OF THE PROPERTY FOR THE POSSIBLE PRESENCE OF ASBESTOS, UNDERGROUND STORAGE TANKS OR HAZARDOUS SUBSTANCES. NO REPRESENTATION OR RECOMMENDATION IS MADE BY THE AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION OR BY THE REAL ESTATE BROKERS OR THEIR CONTRACTORS, AGENTS OR EMPLOYEES AS TO THE LEGAL SUFFICIENCY, LEGAL EFFECT, OR TAX CONSEQUENCES OF THIS LEASE OR THE TRANSACTION TO WHICH IT RELATES; THE PARTIES SHALL RELY SOLELY UPON THE ADVICE OF THEIR OWN COUNSEL AS TO THE LEGAL AND TAX CONSEQUENCES OF THIS LEASE. IF THE SUBJECT PROPERTY IS IN A STATE OTHER THAN CALIFORNIA, AN ATTORNEY FROM THE STATE WHERE THE PROPERTY IS LOCATED SHOULD BE CONSULTED.

The Parties hereto have executed this Lease at the place and on the dates specified above their respective signatures.

Executed at: \_\_\_\_\_ Executed at: \_\_\_\_\_

on: \_\_\_\_\_ on: \_\_\_\_\_

BY LESSOR:

BY LESSEE:

Richard and Donna Piazza, Trustees  
of the Piazza Family Trust

Skechers U.S.A., Inc.

By: /s/ RICHARD PIAZZA  
\_\_\_\_\_

By: /s/ DAVID WEINBERG  
\_\_\_\_\_

Name Printed: Richard Piazza, Trustee  
\_\_\_\_\_

Name Printed: David Weinberg  
\_\_\_\_\_

Title: Owner  
\_\_\_\_\_

Title: CFO  
\_\_\_\_\_

By: /s/ DONNA PIAZZA  
\_\_\_\_\_

By: \_\_\_\_\_

Name Printed: Donna Piazza, Trustee  
\_\_\_\_\_

Name Printed: \_\_\_\_\_

Title: Owner  
\_\_\_\_\_

Title: \_\_\_\_\_

Address: 2612 Pine  
Manhattan Beach, CA 90266  
\_\_\_\_\_

Address: 228 Manhattan Beach Blvd., #200  
Manhattan Beach, CA 90265  
\_\_\_\_\_

Telephone: (310) 545-4203  
\_\_\_\_\_

Telephone: (310) 318-3100  
\_\_\_\_\_

Facsimile: ( ) \_\_\_\_\_

Facsimile: ( ) \_\_\_\_\_

BROKER:

BROKER:

Executed at: \_\_\_\_\_

Executed at: \_\_\_\_\_

on: \_\_\_\_\_

on: \_\_\_\_\_

By: \_\_\_\_\_

By: \_\_\_\_\_

Name Printed: \_\_\_\_\_ Name Printed: \_\_\_\_\_  
 Title: \_\_\_\_\_ Title: \_\_\_\_\_  
 Address: \_\_\_\_\_ Address: \_\_\_\_\_  
 -----  
 Telephone: (\_\_\_\_) \_\_\_\_\_ Telephone: (\_\_\_\_) \_\_\_\_\_  
 Facsimile: (\_\_\_\_) \_\_\_\_\_ Facsimile: (\_\_\_\_) \_\_\_\_\_

NOTE: These forms are often modified to meet changing requirements of law and needs of the industry. Always write or call to make sure you are utilizing the most current form: AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION, 700 South Flower Street, Suite 600, Los Angeles, California 90017. (213) 687-8777.

ADDENDUM TO STANDARD INDUSTRIAL/COMMERCIAL  
 MULTI-TENANT LEASE -- MODIFIED NET  
 BY AND BETWEEN RICHARD AND DONNA PIAZZA,  
 TRUSTEES OF THE PIAZZA FAMILY TRUST AND  
 SKECHERS U.S.A., INC. ("LESSEE")

This Addendum is attached to and made a part of the Lease dated as of July 1, 1999 by and between the above-named Lessor and Lessee, with regard to the leased premises located at 1108 B Manhattan Avenue, Manhattan Beach, California. In the event of a conflict between any provisions contained in the Lease and any provisions contained in this Addendum, the provisions of this Addendum shall control.

49. OPTION TO EXTEND. So long as Lessee is not in default under this Lease, or the lease for the Upstairs Space (as defined in Paragraph 56), or the right of Lessor to exercise the option to extend this Lease as set forth below is not precluded by the occurrence of one (1) or more of the events set forth in Paragraph 39.4 of the Lease, Lessee will have the option to extend the Original Term of this Lease for an additional period of five (5) years ("Option Period") on the same terms, covenants, and conditions of this Lease, except that the Base Rent during the Option Period shall be determined pursuant to Paragraph 50. Lessee will exercise its option by giving Lessor written notice at least one hundred eighty (180) days but not more than two hundred seventy days (270) days prior to the expiration of the Original Term.

50. RENT INCREASES. Commencing July 1, 2000 and on each July 1 thereafter during the Original Term hereof and the Option Period, the Base Rent shall be increased by four percent (4%) of the Base Rent payable during the prior twelve (12) months.

51. BASE RENT UPON EXECUTION. The \$2,709.00 payment upon execution of this Lease represents Base Rent for July 1 through July 31, 1999.

52. AS-IS CONDITION. Lessor shall deliver the Premises to Lessee, and Lessee shall lease from Lessor the Premises in its "as-is" condition as of the Commencement Date. Lessee shall have no obligation to construct any additional improvements to the Premises, or to repair or clean up any portion of the Premises.

53. EXCLUSIONS FROM COMMON AREA OPERATING EXPENSES. Notwithstanding anything to the contrary contained in the Lease, there shall be excluded from Common

Area Operating Expenses the following:

- (1) Costs incurred in connection with the original construction of the Industrial Center or in connection with any major change in the Industrial Center, such as adding or deleting floors;
- (2) Costs of alterations or improvements to the premises of any lessees of the Building;
- (3) Depreciation, interest and principal payments on mortgages, and other debt costs, if any;
- (4) Costs for which Lessor is reimbursed by any insurance carrier;
- (5) Any bad debt loss, rent loss or reserves for bad debts or rent loss;
- (6) Fines, penalties and interest (except as specifically provided in paragraph 19 of this Lease); and
- (7) Tax penalties incurred as a result of Lessor's negligence, inability or unwillingness to make payments when due.

In the calculation of Common Area Operating Expenses, it is understood that no expenses shall be charged more than once. If one lessee's use results in higher insurance premiums on the policies maintained by Lessor hereunder, Lessor agrees to provide an equitable proration thereof in billing the Common Area Operating Expenses. Lessor agrees to keep books and records showing the Common Area Operating Expenses in accordance with a system of accounts and account practices consistently maintained on a year-to-year basis, and to provide Lessee with access thereto upon reasonable notice.

54. Notwithstanding any other provision of the Lease or this Addendum, Lessee acknowledges that the retail businesses at the Building engage in the practice of displaying merchandise in the Common Area in front of their respective premises. Lessee further acknowledges that the other lessees' display of their merchandise in the Common Area shall be acceptable use of the Common Area by other lessees of the Building and shall not be a breach of Lessor's obligation to operate the Common Area in a neat, clean, good order and condition.

55. ASSIGNMENT. Notwithstanding the provisions of paragraph 12, no consent from Lessor shall be required for the assignment or subletting of this Lease under the following circumstances:

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(i) the transfer of stock of Lessee to members of immediate family of a shareholder of Lessee, to a living trust for estate planning purposes, or by will or intestacy; or

(ii) Lessee sells or offers for sale its voting stock to the public in accordance with the qualifications or registration requirements of the State of California and the Security Act of 1933, as amended.

56. Notwithstanding the foregoing, Lessor and Lessee acknowledge that the parties have entered into a separate Commercial Lease Agreement for that certain portion of the Building commonly known as 1110 Manhattan Avenue, Manhattan Beach, CA ("Upstairs Space").

57. LESSEE'S SIGN. In addition to the obligations of Lessee with respect to the placement of a sign upon the exterior of the Premises ("Lessee's Sign") and Lessee's adherence to the signage criteria established for the Building by Lessor, Lessee's Sign shall conform with the signs of the other retail lessees at the Building.

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suppliers at the Premises, Building and Real Property, and, if necessary, Tenant shall employ union labor to achieve such harmonious relations.

6.6 Hazardous Materials. If the construction of the Tenant Improvements or Tenant's move into the Premises will involve the use of or disturb hazardous materials or substances existing in the Premises, Tenant shall comply with Landlord's rules and regulations concerning such hazardous materials or substances.

## SUBSIDIARIES OF THE REGISTRANT

Name of Subsidiary -----	State of Incorporation/Organization -----
Skechers By Mail, Inc.	Delaware
Skechers U.S.A., Inc. II	Delaware
Skechers Collection LLC	California
Skechers Sport LLC	California



INDEPENDENT AUDITOR'S CONSENT

The Board of Directors  
Skechers U.S.A., Inc.:

We consent to the incorporation by reference in the registration statement on Form S-8 (Nos. 333-87009 and 333-87011) of Skechers U.S.A., Inc. of our report dated February 29, 2000 with respect to the consolidated balance sheets of Skechers U.S.A., Inc. and subsidiaries as of December 31, 1999 and 1998, and the related consolidated statements of earnings, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 1999, which report appears in the December 31, 1999, annual report on Form 10-K of Skechers U.S.A., Inc.

KPMG LLP

Los Angeles, California  
March 27, 2000

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</FN>