

AS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ON MARCH 26, 1999.  
REGISTRATION NO. 333-75137

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

AMENDMENT NO. 1  
TO

FORM SB-2  
REGISTRATION STATEMENT  
UNDER  
THE SECURITIES ACT OF 1933

Pacific Softworks, Inc.

(Name of small business issuer in its charter)

California	8980	77-0390628
----- (State or Other Jurisdiction of Incorporation or Organization)	----- (Primary Standard Industrial Classification Code Number)	----- (I.R.S. Employer Identification No.)

703 Rancho Conejo Boulevard  
Newbury Park, California 91320  
(805) 499-7722

(Address and Telephone Number of Principal Executive Offices and  
Address of Principal Place of Business or Intended Principal Place of Business)

Glenn P. Russell  
President and Chief Executive Officer  
Pacific Softworks, Inc.  
703 Rancho Conejo Boulevard  
Newbury Park, California 91320  
(805) 499-7722

(Name, Address and Telephone Number of Agent For Service)

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Approximate date of commencement of proposed sale to the public: As soon as practicable following the date on which this registration statement becomes effective.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended, check the following box. [X]

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act of 1933, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ]

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act of 1933, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ]

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act of 1933, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [ ]

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. [ ]

CALCULATION OF REGISTRATION FEE

Title of Each Class Of Securities To Be Registered -----	Amount To Be Registered(1) -----	Proposed Maximum Offering Price Per Unit(2) -----	Proposed Maximum Aggregate Offering Price -----	Amount Of Registration Fee -----
Units, each comprising one share of common stock and one warrant(3)(4)	920,000	\$ 5.25	\$ 4,830,000	\$1,342.74
(a) Common stock	920,000	--	--	--
(b) Warrants to purchase common stock	920,000	--	--	--
(c) Common Stock	920,000	\$ 7.50	\$ 6,900,000	\$1,918.20
Underwriter's option for the purchase of units comprising one share of common stock and one warrant(4)(5)	1 Warrant		\$ 100	\$ 1.00
Units, underlying underwriter's option each comprising one share of common stock and one warrant(4)(5)	80,000	\$ 6.30	\$ 504,000	\$ 140.11
(a) Common stock	80,000	--	--	--
(b) Warrants to purchase common stock	80,000	--	--	--
(c) Common stock	80,000	\$ 7.50	\$ 600,000	\$ 166.80
Units, each comprising one share of common stock and one warrant(4)(6)	80,000	\$ 5.25	\$ 420,000	\$ 116.76
(a) Common stock	80,000	--	--	--
(b) Warrants to purchase common stock	80,000	--	--	--
(c) Common stock	80,000	\$ 7.50	\$ 600,000	\$ 166.80
Common stock(7)	200,000	\$ 5.25	\$ 1,050,000	\$ 291.90
Total			\$14,904,100	\$4,144.31

- (1) Assumes the underwriter's over-allotment option is exercised in full.
- (2) Estimated pursuant to Rule 457(o) under the Securities Act solely for the purpose of calculation of the registration fee.
- (3) Includes 920,000 shares of common stock issuable upon exercise of the warrants.
- (4) Pursuant to Rule 416 promulgated under the Securities Act of 1933, as amended, an indeterminate number of additional shares of common stock are registered hereunder in the event that provisions preventing dilution are triggered, as provided in the warrants. No additional registration fee has been paid for these shares of common stock.
- (5) Shares of common stock and warrants to purchase common stock included in the units issuable on exercise of the underwriter's option for the purchase of units.
- (6) Shares of common stock and warrants to purchase common stock issuable on exercise of warrants to acquire 80,000 units and also includes 80,000 shares of common stock issuable upon exercise of the warrants.
- (7) Shares of common stock registered on behalf of certain registering stockholders.

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment that specifically states that this registration statement shall thereafter become effective in accordance with section 8(a) of the Securities Act of 1933, as amended, or until the registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to such section 8(a), may determine.

## EXPLANATORY NOTE

This registration statement contains two prospectuses.

The first prospectus forming a part of this registration statement is to be used in connection with the underwritten public offering of 920,000 units, including 120,000 units subject to the underwriter's over-allotment option. Each unit consists of one share of common stock and one warrant. The first prospectus immediately follows this explanatory note.

The second prospectus forming a part of this registration statement is to be used in connection with the resale named stockholders and consultants to Pacific Softworks of:

- up to 80,000 units issuable upon exercise of their warrants to purchase units, and
- up to 200,000 shares of common stock.

The second prospectus will consist of:

- the cover page and inside cover page immediately following the first prospectus,
- pages 1 through 57, other than the section entitled "Underwriting," and pages F-1 through F-15 of the first prospectus,
- pages SS-1 through SS-3,
- page SS-2 which will appear in place of the section entitled "Underwriting," and
- the back cover page, which immediately follows the inside back cover page of the first prospectus.

The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission or any applicable state securities commission becomes effective. This preliminary prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

PROSPECTUS

Subject to completion, dated May \_\_, 1999

800,000 UNITS

[PACIFIC SOFTWARES, INC. LOGO]

CONSISTING OF 800,000 SHARES OF COMMON STOCK  
AND  
800,000 WARRANTS

This is our initial public offering of securities. We expect that the initial public offering price per unit will be between \$5.00 and \$5.50. Each unit consists of one share of common stock and one warrant. The common stock and warrants will trade separately. The public offering price may not reflect the market price of our securities after the offering.

Each warrant allows its holder to purchase for a period of 24 months one share of common stock at a price of \$7.50. We reserve the right to redeem all outstanding warrants at \$0.05 per warrant if the closing bid price of our common stock equals or exceeds \$8.00 per share for 15 consecutive trading days.

We expect to list the common stock and warrants on the Nasdaq SmallCap Market under the symbols "PASw" and "PASWw."

By a separate prospectus concurrent with this offering security holders who are not officers or directors will offer for sale up to 80,000 units and 200,000 shares of common stock. We will not receive any proceeds from the sale of these securities.

INVESTING IN OUR SECURITIES INVOLVES A HIGH DEGREE OF RISK. SEE "RISK FACTORS" BEGINNING ON PAGE 6.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED THESE SECURITIES OR PASSED UPON THE ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The underwriter has a 45-day option to purchase an additional 120,000 units from Pacific Softworks.

	Per Unit -----	Without Over-Allotment -----	With Over-Allotment -----
Price to public	\$	\$	\$
Underwriting discounts	\$	\$	\$
Pacific Softworks' proceeds	\$	\$	\$

The underwriter is offering the units on a firm commitment basis and expects to deliver the units against payment in Los Angeles, California on \_\_\_\_\_, 1999.

SPENCER EDWARDS, INC.

May \_\_, 1999

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## PROSPECTUS SUMMARY

This summary highlights only selected information contained elsewhere in this prospectus. Before making an investment in the securities of Pacific Softworks you should read this entire prospectus and the financial statements and notes, all of which should be consulted when reading this summary.

## PACIFIC SOFTWORKS, INC.

## OUR BUSINESS

Pacific Softworks develops and licenses Internet and Web related software and software development tools. Our products enable Internet and Web based communications, based on a set of rules known as protocols, and are embedded into systems and "information appliances" developed or manufactured by others. Information appliances are Internet connected versions of everyday products such as telephones, televisions, fax machines and other digitally based devices.

Rapid advances are enabling wired and wireless information appliances to assume many of the tasks now handled by personal computers. We believe that Web browsing enabled by embedded software in information appliances used by businesses and individuals will be a major market. International Data Corp. estimates that 94% of Internet access is now made through PCs. By 2002, that percentage is expected to decrease to 64% and the number of information appliances sold is expected to exceed the number of PCs sold.

We intend to evolve and refine our business to track the growth of embedded software in information appliances that incorporate Internet and Web communications capabilities. As information appliances proliferate, we anticipate that our opportunities for long term revenue growth will also increase.

Our Internet and Web related software development tools offer significant benefits to our customers including:

- Accelerated product development and market entry,
  
- Portability across multiple hardware and software system environments, and
  
- Comprehensive embedded solutions that enable information appliances to connect with the Internet and use the Web.

Information appliance manufacturers and software developers have included our products within the following applications and information appliances:

Applications - - - - -	Information Appliances - - - - -
- - Office automation	- Internet fax, copiers, laser printers, scanners
- - Medical	- Patient monitors, imaging systems
- - Multimedia	- DVD players, projectors, digital cameras
- - Industrial controls	- Vending machines, traffic controls, scoring systems, security controls
- - Networking	- Routers, switches, network controls, cable modems
- - Set-top boxes	- Set-top boxes, Internet TV
- - Wireless	- Telephones, personal digital assistants, pagers, electronic organizers
- - Navigation systems	- Navigational controls, air traffic controls
- - Defense and aerospace	- Engine controls, smart weapons
- - Satellite	- Satellite positioning, uplink and downlink of streaming video

We have developed a new proprietary Internet browser for use within independent, "non-Windows(R)" information appliances. We expect to begin marketing this browser, under the "FUSION WebPilot Micro Browser(TM)" name, during the third quarter of 1999. Our browser may be effectively placed in use without an operating system and does not require substantial amounts of memory. We believe that our browser may prove particularly attractive to manufacturers of information appliances who would rather give their products a proprietary or subjective "look and feel" than to be restricted by a browser which requires or depends on the "look and feel" of commercially available operating systems such as Windows(R).

#### OUR CUSTOMERS

Since incorporation in 1992, we have licensed our products to over 400 companies around the world, including: Alcatel, AT&T, America OnLine, Canon, Canal+, Cisco, Cocom, Bell Labs, Data General, Concurrent Technologies, Ericsson, General Instruments, Hughes, Honeywell, Hewlett Packard, Intel, Motorola, Newbridge, Nortel, Psion, Philips, Samsung, Siemens, ST Microsystems, Tandberg, Unisys, and VLSI.

#### OUR REVENUE MODEL

We have historically licensed our source code for a one time fee. Depending on the products and their use, this one-time fee typically ranged from \$10,000 to \$40,000. We anticipate that our revenue model for new products will evolve into one based primarily on royalties measured against our customers' units of production.

#### GENERAL

"Pacific Softworks," "FUSION," "WebPilot," "FastTrack," "WebWatch," "FusOS," "AirMail," "SimpleMail" and "FusionWizard" are all trademarks of Pacific Softworks. All other trade names, trademarks and service marks appearing in this prospectus are the property of their respective holders.



Our executive offices are located at 703 Rancho Conejo Boulevard, Newbury Park, California 91320 and our telephone number is (805) 499-7722. Our Web site address is [www.pacificsw.com](http://www.pacificsw.com). Information contained on our Web site does not constitute part of this prospectus.

#### THE OFFERING

Units offered:	800,000, each consisting of one share of common stock and one warrant.
Warrant attributes:	Each warrant entitles the holder to purchase one share of common stock for \$7.50 for the 24 months ending _____, subject to our rights to redeem warrants at \$0.05 per warrant if the closing bid price of our common stock equals or exceeds \$8.00 per share for 15 consecutive trading days.
Risk factors:	Investing in our securities involves a high degree of risk. You should read "Risk Factors" beginning on page 6 as well as other cautionary statements throughout this prospectus to insure you understand the risks associated with an investment in our securities.
Dividend policy:	Pacific Softworks does not intend to pay dividends.
Proposed Nasdaq SmallCap Market symbols:	Common stock: PASW Warrants: PASWW
Use of proceeds:	We estimate that we will receive net proceeds of about \$3,500,000. We expect to use net proceeds for research and development of our Web products, enhancements to existing Internet and application products, expansion of marketing and sales capabilities, intellectual property protection and working capital.
Common stock to be outstanding after the offering:	4,100,000 shares.

In addition to 4,100,000 shares of common stock outstanding after the offering, Pacific Softworks may issue 800,000 shares of common stock on exercise of the warrants and 665,000 shares of common stock on exercise of currently outstanding options and warrants.

Concurrent with this offering we have also prepared a separate prospectus for security holders who are not officers or directors so that they may sell up to 80,000 units and 200,000 shares of common stock. We will not receive any proceeds from the sale of these securities. The security holders have agreed with the underwriter not to sell their securities for 13 months without the prior written consent of the underwriter.

Except where noted otherwise, all information in this prospectus, including share and per share information, assumes no exercise of the underwriter's over-allotment option.

## SUMMARY CONSOLIDATED FINANCIAL DATA

## CONSOLIDATED STATEMENTS OF OPERATIONS DATA:

	Year Ended December 31,		Unaudited Three Months Ended March 31,	
	1997	1998	1998	1999
	(In thousands except per share data)			
Net revenue .....	\$ 3,310	\$ 2,787	\$ 696	\$ 772
Gross profit .....	3,193	2,687	668	741
Selling, general and administrative .....	2,110	1,936	386	381
Research and development .....	834	852	214	324
Depreciation and amortization .....	64	59	15	13
Former officer's consulting and administrative expense .....	314	314	82	82
Loss from operations .....	(129)	(474)	(29)	(59)
Net loss .....	\$ (129)	\$ (474)	\$ (29)	\$ (59)
	=====	=====	=====	=====
Net loss per share, basic and diluted .....	\$ (0.04)	\$ (0.14)	\$ (0.01)	\$ (0.02)
	=====	=====	=====	=====

The following table indicates a summary of our balance sheet as of March 31, 1999. The column labeled "as adjusted" reflects our receipt of estimated net proceeds from the sale of 800,000 units at an assumed initial public offering price of \$5.25 per unit, after deducting underwriting discounts and estimated expenses.

## CONSOLIDATED BALANCE SHEET DATA:

	Unaudited March 31, 1999	
	Actual	As Adjusted
	(in thousands)	
Cash and cash equivalents	\$ 461	\$3,947
Working capital .....	546	4,032
Total assets .....	1,331	4,817
Total stockholders' equity	819	4,305

## RISK FACTORS

The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties of which we are unaware or which we currently deem immaterial also may become important factors that may adversely affect us.

If any of the following risks actually occur, our business, financial condition or operating results could be materially and adversely affected. In this case, the trading price of our securities could decline, and you may lose all or a part of your investment.

WE HAVE REPORTED LOSSES FOR OUR LAST TWO YEARS AND FOR THE THREE MONTHS ENDED MARCH 31, 1999.

We reported losses of \$129,000 and \$474,000 for the years ending December 31, 1997 and 1998. These losses include about \$314,000 paid during each of those years for former officer's consulting and administrative expense. We also reported losses of \$29,000 and \$59,000 for the three months ended March 31, 1998 and 1999. These losses include \$82,000 paid during each of those calendar quarters for former officer's consulting and administrative expense. As of May 1999 we will pay that former officer approximately \$131,000, in equal monthly installments through September 1999. We can provide no assurance that we will be profitable in the future.

BECAUSE WE EXPECT THAT OUR OPERATING RESULTS WILL CONTINUE TO FLUCTUATE, YOU SHOULD NOT RELY ON THE RESULTS OF ANY PERIOD AS AN INDICATION OF FUTURE PERFORMANCE.

From time to time we have experienced material period-to-period fluctuations in revenue and operating results. We anticipate that these periodic fluctuations in revenue and operating results will occur in the future. We attribute these fluctuations to a variety of business conditions that include:

- the volume and timing of orders received during the quarter,
- the timing and acceptance of new products and product enhancements by us and our competitors,
- unanticipated sales and buyouts of run-time licenses,
- stages of product life cycles,
- purchasing patterns of customers and distributors,
- market acceptance of products sold by our customers, and
- competitive conditions in our industry.

As a result of the factors described above we believe that quarterly revenue and operating results are likely to vary significantly in the future and that quarter to quarter comparisons of our operating results may not be meaningful. You should therefore not rely on the results of one quarter as an indication of future performance.

BECAUSE WE DEPEND ON A SMALL NUMBER OF LARGE ORDERS, THE LOSS OR DEFERRAL OF ORDERS MAY HAVE A NEGATIVE IMPACT ON REVENUES WHICH COULD LOWER THE VALUE OF OUR SHARES.

Although no customer has accounted for 10% or more of total revenue in any fiscal year, we derive a significant portion of our software license revenue in each quarter from a small number of relatively large orders. While we believe that the loss of any particular customer is not likely to have a material adverse effect on our business, our operating results could be materially adversely affected if we were unable to complete one or more substantial license sales in any future period.

BECAUSE WE RELY ON A CORE SUITE OF PRODUCTS AND NEW PRODUCTS, ANY DECREASE IN THE MARKET ACCEPTANCE OF OUR INTERNET AND WEB PRODUCTS WOULD DECREASE OUR REVENUE AND LOWER THE VALUE OF YOUR INVESTMENT.

Our future results depend heavily on continued market acceptance of our products in existing and new markets. Revenue from licenses of our suite of Internet and Web products and sales of our services accounted for all of our revenue in the year ended December 31, 1998. Our research and development expenditures for 1997 and 1998 resulted in several new products. We introduced FastTrack(TM) in November 1998 and expect to market our FUSION WebPilot Micro Browser(TM) by mid 1999. We cannot give any assurances that these products will be accepted by our customers.

OUR RECENTLY ADOPTED PRICING STRATEGY FOR NEW WEB PRODUCTS BASED ON FLEXIBLE UP-FRONT FEES WITH ONGOING ROYALTIES MAY NOT RESULT IN INCREASED REVENUES WHICH COULD REDUCE THE VALUE OF YOUR INVESTMENT.

Historically we have charged a one-time fee for a source code license and have occasionally also charged royalties for each copy of our software embedded in our customers' products. Our recently formulated strategy for new products is to seek flexible up-front fees with ongoing royalties measured against our customers' units of production or run times. Any increase in the portion of revenue attributable to royalties will depend on our successful negotiation of royalty agreements and on the successful commercialization by our customers of their underlying products.

BECAUSE WE LACK THE NAME RECOGNITION, CUSTOMER BASE AND RESOURCES OF OTHER COMPANIES IN THE INTERNET SOFTWARE MARKET, WE MAY BE UNABLE TO COMPETE SUCCESSFULLY WHICH WOULD REDUCE OUR REVENUES AND THE VALUE OF YOUR INVESTMENT.

The markets for our products are intensely competitive, and are likely to become even more competitive. Increased competition could result in:

- pricing pressures, resulting in reduced margins,
- decreased volume, resulting in reduced revenue, or
- the failure of our products to achieve or maintain market acceptance.

Any of these occurrences could have a material adverse effect on our business, financial condition and operating results. Each of our products faces intense competition from multiple competing vendors. Our principal competitors include Wind River Systems, Inc., Integrated Systems, Inc., Mentor Graphics, Inc., Microware Systems Corporation and Microsoft Corporation. Many of our current and potential competitors have:

- longer operating histories,
- greater name recognition,

- access to larger customer bases, or
- substantially greater resources than we have.

As a result, our principal competitors may respond more quickly than we can to new or changing opportunities and technologies. For all of the reasons stated above, we may be unable to compete successfully against our current and future competitors.

IF WE ARE UNABLE TO RAISE MARKET AWARENESS OF OUR FUSION BRAND, WE MAY EXPERIENCE A MATERIAL ADVERSE EFFECT ON OUR OPERATING RESULTS WHICH WOULD DIMINISH THE VALUE OF YOUR INVESTMENT.

If we fail to promote our brand successfully or if we incur significant expenses promoting and maintaining our FUSION brand names, we may experience a material adverse effect on our business, financial condition and operating results. Due in part to the still emerging nature of the market for Internet and embedded software products and the substantial resources available to many of our competitors, we may have a time limited opportunity to achieve and maintain market share. We believe that developing and maintaining awareness of the FUSION brand names will be critical to achieving widespread acceptance of our products. We believe that brand recognition will become increasingly important as competition in the market for our products increases. Successfully promoting and positioning our brand will depend largely on the effectiveness of our marketing efforts and our ability to develop reliable and useful products at competitive prices. As a result, we may need to expand our financial commitment to creating and maintaining brand awareness among potential customers.

WE MAY NOT BE ABLE TO DEVELOP ACCEPTABLE NEW PRODUCTS OR ENHANCEMENTS TO OUR EXISTING PRODUCTS AT THE RATE REQUIRED BY OUR RAPIDLY CHANGING MARKET.

Our future success depends upon our ability to address the rapidly changing needs of our customers by developing and introducing high quality products, product enhancements and services on a timely basis and by keeping pace with technological developments and emerging industry standards. The markets for our products are rapidly evolving. Failure to develop and release enhanced or new products, or delays or quality problems in doing so, could have a material adverse effect on our business, financial condition and operating results.

As is common in new and rapidly evolving industries, demand and market acceptance for recently introduced products are subject to high levels of uncertainty and risk. Furthermore, new products can quickly render obsolete products that were only recently in high demand. The market for our existing products may not be sustainable at its current level. We launched several new products in calendar 1998 and January 1999. We have additional new product launches, as well as upgrades to our existing products, planned for 1999. The market for our recently introduced and planned products may not develop or grow. If the market for these products does not develop or grow we will experience a material adverse effect on our business, financial condition and operating results.

BECAUSE WE PLAN TO DEVOTE SIGNIFICANT FINANCIAL AND MANAGEMENT RESOURCES TO EXPAND SALES AND MARKETING ACTIVITIES OVER THE NEXT 18 MONTHS WE WILL INCUR SUBSTANTIAL ADDITIONAL OPERATING EXPENSES WHICH MAY NOT RESULT IN MEANINGFUL REVENUE INCREASES.

To expand our business, we plan to hire additional product engineering, sales and marketing personnel. Any new hires will require training and may take six months or more to achieve full productivity. We may not be able to hire enough qualified individuals when needed, or

at all. We can give you no assurance that our added operating expense from these activities will result in meaningful revenue increases.

BECAUSE WE RELY ON A SMALL MANAGEMENT TEAM TO OVERSEE OPERATIONS AND GROWTH, THE LOSS OF OUR PRESIDENT OR OTHER KEY PERSONNEL COULD ADVERSELY AFFECT OUR BUSINESS AND DECREASE THE VALUE OF YOUR INVESTMENT.

We depend upon the continued services of a few executive officers and other key management and development personnel. In particular, we rely on Glenn P. Russell, president and chief executive officer, Mark Sewell, vice president, and Sandra J. Garcia, vice president. Glenn P. Russell, Mark Sewell and Sandra J. Garcia do not have employment agreements with Pacific Softworks and, therefore, could terminate their employment with us at any time. We do not maintain key person life insurance policies on any of our employees. The loss of the services of one or more of our executive officers, engineering personnel, or other key employees could have a material adverse effect on our business, financial condition and operating results.

IF OUR EFFORTS TO PROTECT OUR INTELLECTUAL PROPERTY RIGHTS IN OUR INTERNET AND WEB SOFTWARE PRODUCTS ARE UNSUCCESSFUL WE MAY EXPERIENCE AN ADVERSE MATERIAL EFFECT ON OUR OPERATIONS WHICH WOULD REDUCE THE VALUE OF YOUR INVESTMENT.

We regard substantial elements of our Internet and embedded software products as proprietary and attempt to protect them by relying on:

- copyright,
- trade secret and trademark laws,
- nondisclosure, and
- other contractual restrictions on copying, distribution and technical measures.

Any steps we take to protect our intellectual property may be inadequate, time consuming, and expensive.

Despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property. Any infringement or misappropriation of our intellectual property by third parties could have a material adverse effect on our business, financial condition and operating results.

We currently have no issued patents. We believe that one or more features of our software technology are unique and may be patentable. We expect to devote a portion of the proceeds from this offering to seek patent protection for these features. We have no patent applications pending. New patent applications may not result in issued patents and may not provide us with any competitive advantages, or may be challenged by third parties. Legal standards relating to the validity and enforceability of intellectual property rights in Internet-related industries are uncertain and still evolving.

The future viability or value of any of our intellectual property rights is uncertain. Effective trademark, copyright, and trade secret protection may not be available in every country in which our products are distributed or made available through the Internet. Furthermore, our competitors may independently develop similar technology that adversely affects the value of our intellectual property.

**WE MAY INCUR SUBSTANTIAL COSTS IN CONNECTION WITH INTELLECTUAL PROPERTY INFRINGEMENT CLAIMS THAT OTHERS MAY BRING AGAINST US.**

In addition to the technology we have developed internally, we use code libraries developed and maintained by third parties and have acquired or licensed technologies from other companies. Our internally developed technology, the code libraries, or the technology we acquire or license may infringe on the intellectual property rights of others. These persons may bring claims against us alleging infringement of their intellectual property rights. If we infringe or others bring claims against us alleging infringement, our business, financial condition and operating results could be materially and adversely affected.

In recent years, there has been significant litigation in the United States involving patents and other intellectual property rights. We are not currently involved in any intellectual property or other material litigation. We may, however, be a party to litigation in the future to protect our intellectual property or as a result of an alleged infringement of the intellectual property of others. These claims and any resulting litigation could subject us to significant liability for damages and invalidation of our proprietary rights. Litigation, regardless of its success, would likely be time-consuming and expensive to prosecute or defend and would divert management attention from our business. Any potential intellectual property litigation could also force us to do one or more of the following:

- cease selling, incorporating, or using products or services that incorporate the challenged intellectual property,
- obtain from the holder of the infringed intellectual property right a license to sell or use the relevant technology, which license may not be available on reasonable terms, or at all, and
- redesign those products or services that incorporate the infringed intellectual property.

Any of these events could have a material adverse effect on our business, financial condition and operating results.

**IF OUR PRODUCTS ARE DEFECTIVE WE MAY LOSE CUSTOMERS AND ENCOUNTER PRODUCT LIABILITY CLAIMS THAT WOULD REQUIRE CONSIDERABLE EFFORT AND EXPENSE TO DEFEND.**

Our products provide functions that are often critical to the performance of information appliances. The occurrence of errors or failures in our products could result in adverse publicity, loss of or delay in market acceptance, or claims by customers against us, any of which could have a material adverse effect on our business, financial condition and operating results.

Our end-user licenses contain provisions that limit our exposure to product liability claims, but these provisions may not be enforceable in all jurisdictions. Additionally, we maintain limited product liability insurance. To the extent our contractual limitations are unenforceable or if claims are not covered by insurance, a successful product liability claim could have a material adverse effect on our business, financial condition and operating results.

Although we have not experienced any product liability or economic loss claims, our products and product enhancements are very complex and may from time to time contain errors or result in failures that we did not detect or anticipate. The computer hardware environment is characterized by a wide variety of non-standard configurations that make pre-release testing for

programming or compatibility errors very difficult and time consuming. Despite our testing, errors may be discovered in new products or enhancements that we deliver to customers.

ALTHOUGH WE BELIEVE THAT ALL OF OUR PRODUCTS ARE YEAR 2000 COMPLIANT, WE MAY BE ADVERSELY AFFECTED IF OUR CUSTOMERS' PRODUCTS ARE NOT YEAR 2000 COMPLIANT.

If our customers have material sales decreases or other disruptions because their products are not year 2000 compliant, we may experience reduced license fees and royalty income resulting in a material adverse impact on our operations.

OUR SUCCESS DEPENDS ON CONTINUED USE AND EXPANSION OF THE INTERNET.

Continued expansion in the sales of our Internet based embedded software products will depend upon the adoption of the Internet as a widely used medium for commerce and communication. If the Internet does not continue to become a widespread communications medium and commercial marketplace, demand for our products could be significantly reduced, which could have a material adverse effect on our business, financial condition and operating results.

The Internet may prove not to be a viable commercial marketplace for us because of inadequate development of the necessary infrastructure or timely development of complementary products such as high speed modems. The Internet infrastructure may not be able to support the demands placed on it by continued rapid growth. The Internet also could lose its viability as a result of delays in the development or adoption of new standards and protocols to address issues such as Internet:

- activity,
- security,
- reliability,
- cost,
- ease of use,
- accessibility, and
- quality of service.

BECAUSE WE DERIVE MORE THAN 50% OF OUR REVENUE FROM SALES OUTSIDE OF NORTH AMERICA, WE ARE SUBJECT TO MATERIAL RISKS ASSOCIATED WITH INTERNATIONAL MARKETS.

Our international operations are subject to various risks, including:

- foreign government regulation,
- foreign currency fluctuations which could reduce our revenue in dollar terms or make our products more expensive,
- more prevalent software piracy,
- longer payment cycles,
- unexpected changes in regulatory requirements, tariffs, import and export restrictions and other barriers and restrictions,



- greater difficulty in accounts receivable collection,
- potentially adverse tax consequences including restrictions on repatriation of earnings,

- the burdens of complying with a variety of foreign laws,
- difficulties in staffing and managing foreign operations,
- political and economic instability,
- changes in diplomatic and trade relationships, and
- possible recessionary environments in economies outside the United States.

These factors may have a material adverse effect on our international sales and, consequently, our business, operating results and financial condition.

IF WE CHOOSE TO EXPAND THROUGH ACQUISITIONS OF COMPANIES AND TECHNOLOGIES, OUR FUTURE LIQUIDITY AND PROFITABILITY MAY BE ADVERSELY AFFECTED.

Following the offering we may actively consider making acquisitions of, or investments in, other companies, products, technologies or Internet-related services. We may have to expend cash and incur debt or issue equity securities to pay for any future acquisitions. The issuance of equity securities for any acquisition could be substantially dilutive to our stockholders. Our liquidity and profitability also may suffer because of acquisition-related costs or amortization costs for acquired goodwill and other intangible assets.

If we make any acquisitions, we will be required to assimilate the operations, products and personnel of the acquired businesses and train and retain key personnel from the acquired businesses. We may be unable to maintain uniform procedures and policies if we fail in these efforts. Similarly, acquisitions may cause disruptions in our operations and divert management's attention from day-to-day operations. This could impair our relationships with our current employees, customers and strategic partners.

WE MAY APPLY THE PROCEEDS OF THIS OFFERING AND THE PROCEEDS FROM EXERCISE OF WARRANTS TO USES THAT DO NOT INCREASE OUR PROFITS OR MARKET VALUE.

The net proceeds from the sale of our securities will be used primarily for research and development, marketing, sales and general working capital. We may also obtain up to \$6,000,000 from exercise of warrants. The proceeds from any exercise of warrants will be added to our general working capital. Our management will have considerable discretion in the application of the net proceeds added to our general working capital, and you will not have the opportunity, as part of your investment decision, to assess whether the proceeds are being used appropriately. The net proceeds may be used for corporate purposes that do not increase our profitability or market value.

WE MAY HAVE FUTURE CAPITAL NEEDS AND IT IS UNCERTAIN IF WE CAN OBTAIN ADDITIONAL FINANCING.

We expect that the net proceeds from this offering, cash on hand, cash equivalents and commercial credit facilities will be adequate to meet our working capital and capital expenditure needs for about the next 18 months. After that, we may require additional funds for product development, market support and additional expansion.

We can provide no assurance that the warrants will be exercised. We cannot be certain that additional financing will be obtained on favorable terms, if at all. If we cannot raise needed funds on acceptable terms, we may be unable to:

- develop or enhance products,

- take advantage of future opportunities, or
- respond to competitive pressures or unanticipated capital requirements.

The occurrence of any of these events could have a material adverse effect on Pacific Softworks.

FUTURE NON-PUBLIC SALES OF OUR SECURITIES MAY BE ON TERMS MORE FAVORABLE THAN THOSE OF THIS OFFERING.

In order to raise additional working capital, we could sell our common stock or other securities to qualified investors in transactions that are exempt from registration under the securities laws. These purchasers may acquire our securities on terms more favorable than those offered to you in this offering.

BECAUSE OWNERSHIP IS CONCENTRATED, YOU AND OTHER INVESTORS MAY NOT BE ABLE TO INFLUENCE STOCKHOLDER DECISIONS.

Our officers and directors will beneficially own 74.3% of the outstanding common stock after this offering. If all the warrants are exercised, our officers and directors will own 62.6% of the outstanding common stock. Our officers and directors will be able to exercise control over all matters requiring stockholder approval, and you and other investors will have minimal influence over the election of directors or other stockholder actions. As a result, our officers and directors could approve or cause Pacific Softworks to take actions of which you disapprove or that are contrary to your interests. This ability to exercise control over all matters requiring stockholder approval could prevent or significantly delay another company from acquiring or merging with us at prices and terms that you might find to be attractive.

ISSUANCE OF OUR AUTHORIZED PREFERRED STOCK MAY DISCOURAGE A CHANGE IN CONTROL AND REDUCE THE MARKET PRICE OF OUR COMMON STOCK.

The issuance of preferred stock may have the effect of delaying, deferring, or preventing a change in control. Any such issuance may materially and adversely affect the market price of the common stock and the voting rights of the holders of common stock. The issuance of preferred stock may also result in the loss of the voting control of holders of common stock to the holders of preferred stock.

TRADING IN OUR COMMON STOCK AND WARRANTS MAY BE LIMITED AND COULD NEGATIVELY AFFECT YOUR ABILITY TO SELL YOUR SECURITIES.

A public market for our common stock and our warrants has not existed before this offering. Although this offering will result in a trading market for our common stock and warrants, we do not know how liquid that market might be. The initial public offering price for the units will be determined through negotiations between the underwriter and us. If you purchase units, you may not be able to resell these securities at or above the initial public offering price.

THE MARKET PRICES FOR OUR SECURITIES, LIKE THOSE OF OTHER TECHNOLOGY ISSUES, MAY BE VOLATILE.

The value of your investment in Pacific Softworks could decline from the impact of any of the following factors:

- changes in market valuations of Internet software companies,
- variations in our actual and anticipated operating results,

- changes in our earnings estimates by analysts,
- our failure to meet analysts' performance expectations, and
- lack of liquidity.

The stock markets have in general, and with respect to Internet companies in particular, recently experienced stock price and volume volatility that has affected companies' stock prices. The stock markets may continue to experience volatility that may adversely affect the market price of our securities.

Stock prices for many companies in the technology and emerging growth sector have experienced wide fluctuations that have often been unrelated to the operating performance of those companies. Fluctuations such as these may affect the market prices of our common stock and warrants.

YOU WILL INCUR IMMEDIATE SUBSTANTIAL DILUTION BY PURCHASING SECURITIES IN THIS OFFERING.

The initial public offering price applicable to the common stock included in a unit is expected to be substantially higher than the book value per share of the common stock before the offering. By purchasing securities in this offering you will incur immediate substantial dilution.

YOU MAY INCUR ADDITIONAL DILUTION IF WE ARE COMPELLED TO LITIGATE OR ARBITRATE CLAIMS THAT MAY BE BROUGHT BY A MERCHANT BANKER FOR THE RIGHT TO PURCHASE 10% OF PACIFIC SOFTWORKS AT A PRICE WHICH IS SUBSTANTIALLY LOWER THAN THE VALUATION IN THIS OFFERING.

In April 1999 we were notified that a merchant banker claiming rights under a letter to us dated in June 1998 demanded an option to purchase 10% of Pacific Softworks for \$400,000. Although we believe that there is no merit to this claim, if we are compelled to litigate or arbitrate this demand and if we are not successful in our defense, then, in addition to legal fees and expenses which we may incur, you may experience additional dilution.

OUR WARRANTS ARE SUBJECT TO APPLICABLE SECURITIES LAWS AS WELL AS REDEMPTION.

You will own one warrant for each unit that you purchase. You may only exercise your warrants if a registration statement relating to the common stock underlying the warrants is then in effect and we have complied with applicable state securities laws. We may be unsuccessful in maintaining a current registration statement covering the common stock underlying the warrants. You may be unable to exercise the warrants for this or other reasons. Your warrants may also be redeemed by us for a nominal amount if the closing bid price of our common stock equals or exceeds \$8.00 per share for 15 consecutive trading days. If you do not exercise your warrants prior to the redemption date, you will only be entitled to receive the redemption price of \$0.05 per warrant.

OUR STOCK AND WARRANT PRICES MAY BE AFFECTED BY SHARES ELIGIBLE FOR FUTURE SALE.

The market prices of the common stock and the warrants could decrease as a result of large numbers of shares of common stock being available for sale after the offering. These sales could also make it more difficult for us to raise funds through future offerings. The 3,300,000 shares of common stock outstanding before the offering are subject to certain resale restrictions

under federal securities laws. Holders of these shares have agreed that they will not sell these securities without the consent of the underwriter for 13 months after the date of this prospectus.

**SIGNIFICANT FLUCTUATION IN THE MARKET PRICE OF OUR COMMON STOCK AND WARRANTS COULD RESULT IN SECURITIES CLASS ACTION CLAIMS AGAINST US.**

Securities class action claims have been brought against issuing companies in the past where there has been volatility in the market price of a company's securities. Litigation could be very costly and divert our management's attention and resources. Any adverse determination in litigation could also subject us to significant liabilities. Any or all of these events could have a material adverse effect on our business, financial condition and operating results.

**YOU SHOULD NOT RELY ON OUR FORWARD-LOOKING STATEMENTS.**

This prospectus contains forward-looking statements that involve risks and uncertainties. Discussions containing forward-looking statements may be found in the material set forth under "Prospectus Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," and "Business" as well as within this prospectus generally. In addition, when used in this prospectus, the words "believes," "intends," "plans," "anticipates," "expects," and similar expressions are intended to identify forward-looking statements. Forward-looking statements are subject to a number of risks and uncertainties. Actual results could differ materially from those described in the forward-looking statements as a result of the risk factors set forth in this section and the information provided in this prospectus generally. We do not intend to update any forward-looking statements.

**USE OF PROCEEDS**

Based on an assumed public offering price of \$5.25 per unit, we expect that net proceeds from the sale of the 800,000 units sold in this offering will be approximately \$3,486,000, or \$4,034,100 if the underwriter's over-allotment option is exercised in full.

We intend to use net proceeds as indicated in the following table.

APPLICATION	AMOUNT
- - - - -	- - - - -
Research and development of Web products	\$1,500,000
Enhancements to existing Internet and application products	450,000
Marketing and sales	700,000
Intellectual property protection	100,000
Working capital	736,000
	-----
	\$3,486,000
	=====

We may acquire or invest in complimentary businesses, technologies, services or products and a portion of the net proceeds currently allocated to working capital may be used for such

acquisitions or investments. However, we currently have no understandings, commitments or agreements for any material acquisition or investment.

The description above represents our best estimate of the uses of the net proceeds to be received in this offering, based on current planning and business conditions. However, we reserve the right to change these uses when and if market conditions or unexpected changes in operating conditions occur.

The amounts expended for each use may vary significantly depending upon a number of factors including, but not limited to, amounts we spend to develop and introduce new products and the amount of cash generated by our operations. We believe that our existing capital resources and the net proceeds of this offering will be sufficient to maintain current and planned operations for a period of at least 18 months from the date of this prospectus. Net proceeds not immediately required for the purposes described above will be invested principally in investment grade, interest-bearing securities.

#### DIVIDEND POLICY

We have never declared or paid any cash dividends on our common stock or other securities and do not anticipate paying cash dividends in the foreseeable future. Our line of credit currently prohibits the payment of dividends. A share purchase agreement with a former stockholder also prohibits us from paying certain dividends until all obligations owed to him under the agreement are retired.

#### CAPITALIZATION

The following table sets forth our unaudited capitalization as of March 31, 1999:

- on a historical basis and
- on an as adjusted basis, giving effect to the sale of 800,000 units at an assumed initial public offering price of \$5.25 per unit, after deducting underwriting discounts and estimated offering expenses.

You should read this table together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the financial statements and notes thereto appearing elsewhere in this prospectus.

	March 31, 1999	
	(in thousands)	
	Actual	As Adjusted
	-----	-----
Stockholders' equity:		
Preferred stock, \$0.01 par value; 10,000,000 shares authorized; none issued and outstanding .....	\$     --	\$     --
Common Stock, \$0.001 par value; 50,000,000 shares authorized; 3,300,000 shares issued and outstanding; 4,100,000 shares, as adjusted .....	3	4

Additional paid-in capital.....	875	4,360
Accumulated deficit.....	(42)	(42)
Cumulative adjustment for currency translation.....	(17)	(17)
Total stockholders' equity .....	819	4,305
Total capitalization.....	\$ 819	\$ 4,305
	=====	=====

The information provided above excludes:

- 800,000 shares of common stock issuable upon exercise of warrants,
- 665,000 shares of common stock issuable upon exercise of outstanding options and warrants,
- 160,000 shares of common stock issuable upon the exercise of warrants to acquire units and warrants underlying those units, and
- 80,000 units issuable on exercise of the underwriter's option.

#### DILUTION

At March 31, 1999, unaudited net tangible book value was \$536,710, or \$0.16 per share. Net tangible book value per share represents our net tangible assets less liabilities divided by the shares of common stock outstanding.

After giving effect to our sale of 800,000 units and our receipt of an estimated \$3,486,000 of net proceeds from the offering, based on an assumed offering price of \$5.25 per unit, all of which is attributable to the common stock and none of which is attributable to the warrants, adjusted net tangible book value at March 31, 1999 would have been \$0.98 per share. This amount represents an immediate increase in net tangible book value of \$0.82 per share to existing stockholders and an immediate dilution of \$4.27 per share of common stock to new investors purchasing units in the offering. The following table illustrates per share dilution:

Assumed public offering price per share		\$ 5.25
Net tangible book value prior to the offering	\$ 0.16	
Increase attributable to new investors	0.82	
	-----	
Adjusted net tangible book value after the offering		0.98
		-----
Dilution per share to new investors in this offering		\$ 4.27
		=====

The following table sets forth as of March 31, 1999, the number of shares of common stock purchased from Pacific Softworks, the total consideration paid to Pacific Softworks and the average price per share paid by existing stockholders and new investors purchasing units in the offering, before deducting underwriting discounts and estimated offering expenses:

	Shares Purchased		Total Consideration		Average Price Per Share
	Number	Percent	Amount	Percent	
	-----	-----	-----	-----	-----
Existing stockholders	3,300,000	80.5%	\$ 678,000	13.9%	\$0.21
New investors	800,000	19.5%	4,200,000	86.1%	\$5.25
	-----	-----	-----	-----	-----
Total	4,100,000	100.0%	\$4,878,000	100.0%	
	=====	=====	=====	=====	=====





The information for existing stockholders in the table above excludes shares and warrants issuable upon exercise of outstanding options or warrants, the underwriter's option to purchase units and exercise of the underwriter's over-allotment option. To the extent that currently outstanding options or warrants are exercised at prices below \$5.25, there will be further dilution to new investors.

#### SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data is qualified by reference to and should be read in conjunction with the consolidated financial statements and notes thereto and with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and other financial information included elsewhere in this prospectus. The consolidated statement of operations data for the years ended December 31, 1997 and 1998 and the consolidated balance sheet data at December 31, 1997 and 1998 are derived from and qualified by reference to, audited consolidated financial statements included elsewhere in this prospectus. The consolidated statement of operations data for the three month period ended March 31, 1998 and 1999 and the consolidated balance sheet data at March 31, 1999 have been derived from our unaudited financial statements but have been prepared on the same basis as our audited financial statements which are included in this prospectus. In our opinion, these unaudited financial statements include all adjustments, consisting of normally recurring adjustments considered necessary for a fair presentation of our financial position and results of operations for that period.

## CONSOLIDATED STATEMENTS OF OPERATIONS DATA:

	Year Ended		Unaudited	
	December 31,		Three Months Ended	
	1997	1998	1998	1999
	(in thousands, except per share data)			
Net revenue .....	\$ 3,310	\$ 2,787	\$ 696	\$ 772
Cost of revenue .....	117	100	28	31
Gross profit .....	3,193	2,687	668	741
Selling, general and administrative ..	2,110	1,936	386	381
Research and development .....	834	852	214	324
Depreciation and amortization .....	64	59	15	13
Former officer's consulting and administrative expense .....	314	314	82	82
Total Expense .....	3,322	3,161	697	800
Net loss .....	\$ (129)	\$ (474)	\$ (29)	\$ (59)
Net loss per share, basic and diluted	\$ (0.04)	\$ (0.14)	\$ (0.01)	\$ (0.02)

## CONSOLIDATED BALANCE SHEET DATA:

	December 31,		Unaudited
	1997	1998	March 31,
			1999
	(in thousands)		
Cash and cash equivalents	\$ 625	\$ 224	\$ 461
Working capital .....	761	222	546
Total assets .....	1,071	643	1,331
Total stockholders' equity	691	207	819

See notes 1 and 12 of notes to consolidated financial statements for a discussion regarding the computation and presentation of basic and diluted net loss per share.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis in conjunction with "Selected Financial Data" and the consolidated financial statements and related notes.

## OVERVIEW

Pacific Softworks develops and licenses a suite of embedded Internet and Web software products for business and individual customers that seek to add Internet-based communication capabilities to their information appliances.

In distributing our products, we primarily have licensed source code to our customers for a one time fee. Manufacturers or developers customize their information appliances containing our licensed software to serve a particular need or market.

Our traditional focus and expertise has been on one of the principal building blocks of the Internet, the underlying information transport protocol known as TCP/IP. We have subsequently developed additional products that provide other various essential elements of networked data communication and transport. We have historically derived the majority of our revenue from the licensing of a small range of relatively independent protocols that our customers integrate with their own software products. We are in the process of completing development of a range of embedded products, including an embedded Web browser and related software accessories. These products will provide customer ready solutions for the information appliance and embedded systems market.

Historically, we had no materially significant post sale commitments following software delivery. As a result we recognized revenue upon product shipments to customers. We found that many of our older products were becoming commodity items, with steady price erosion and competition. We could therefore not support royalty bearing licenses on these products.

With the introduction of our new Internet and Web application products, we initiated a plan to charge a one-time fee for a development license and a run-time or per unit production license fee for each copy of these applications used in the customer's products. We intend to follow this approach for many of our new products introduced and expected to be sold in 1999. Any increase in the percentage of revenue attributable to run-time and unit production licenses will depend on our successful negotiation of run-time and unit production license agreements and on the successful commercialization by our customers of their underlying products.

The typical one-time license fee of our base TCP/IP product has been between \$10,000 and \$40,000. Due to competitive pressures and the implementation of upgraded TCP/IP protocols, we expect this average sale amount for our more mature products to decrease by 20% or more per year over the next few years. We expect this decay in pricing and reduced gross profit margins for our mature TCP/IP product line to be partially offset by several factors:

- increased use and thus increased total licenses of TCP/IP,
- availability of the new FastTrack(TM) solutions, which should increase our average license fee by \$10,000,
- availability of our new TCP/IP version 6, which is expected to become available within the next 12 to 18 months, and that may increase our average license to \$80,000, and
- availability of our IP security and encryption products before the end of this fiscal year at prices which we believe will exceed \$80,000 per license.

We anticipate that the FUSION WebPilot Micro Browser(TM) will be priced at approximately \$100,000 per unit and above for the initial license, plus royalties measured against run-time or customer's units of production. We expect to be licensing and delivering this product during the third quarter of 1999.

## RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, the percentage relationship to net revenue of certain items in our consolidated statements of operations and comprehensive income:

	Year Ended December 31,		Unaudited Three Months Ended March 31	
	1997	1998	1998	1999
Net revenue .....	100.00%	100.00%	100.00%	100.00%
Cost of revenue .....	3.51	3.61	4.00	3.93
Gross profit .....	96.49	96.39	96.00	96.07
Selling, general and administrative ...	63.75	69.45	55.52	49.35
Research and development .....	25.20	30.55	30.70	41.97
Depreciation and amortization .....	1.94	2.11	2.11	1.74
Former officer consulting and administrative expense .....	9.50	11.28	11.88	10.71
Total operating expenses .....	100.39	113.39	100.21	103.77
Net loss from operations .....	(3.90)	(17.00)	(4.21)	(7.70)
Foreign currency translation adjustment	1.51	(0.34)	(5.74)	(3.70)
Comprehensive loss .....	(2.39%)	(17.34%)	(9.95%)	11.40%

The following table sets forth, for the periods indicated, the percentage of net revenue by principal geographic area to total revenue:

	Year Ended December 31,		Unaudited Three Months Ended March 31	
	1997	1998	1998	1999
United States .....	48%	42%	58%	43%
United Kingdom and Europe	35	40	38	42
Australia and Asia .....	15	17	3	14
Other .....	2	1	1	1
Total .....	100%	100%	100%	100%
	===	===	===	===

## THREE MONTHS ENDED MARCH 31, 1999 AND 1998

## NET REVENUE

Our net revenue for the three months ended March 31, 1999 increased 11% to \$771,650 from \$696,079 for the three months ended March 31, 1998. The increase in revenue for 1999 was attributable to royalty revenue received from our operations in Japan. The increase in international sales from 42% to 57% is principally due to a decline in domestic sales as a result of increased competition and related price discounting.

## COST OF REVENUE

Our cost of revenue for the three months ended March 31, 1999 totaled \$30,336 compared to \$27,843 for the three months ended March 31, 1998. The cost of revenue in both periods was 4% of net revenue.

## SELLING, GENERAL AND ADMINISTRATIVE EXPENSE

Selling, general and administrative expense decreased from \$386,447 or 56% of revenue in the three months ended March 31, 1998 to \$380,815 or 49% of revenue for the three months ended March 31, 1999. The reduction from period to period reflects a continuing reduction of sales and operating expenses offset in part by increases in corporate consulting expenditures related to strategic planning and marketing and an increase in rent following the relocation of our principal executive offices to our current location in mid 1998.

## RESEARCH AND DEVELOPMENT EXPENSE

Our research and development expense increased from \$213,703 or 31% of revenue to \$323,824 or 42% of revenue for the three months ended March 31, 1998 compared to the three months ended March 31, 1999. The increase in research and development expense in 1999 was principally attributable to a continuation of development of the FastTrack product line and the beginning of development of the FUSION WebPilot Micro Browser(TM) in 1998.

## DEPRECIATION AND AMORTIZATION EXPENSE

Depreciation and amortization expense decreased from \$14,713 to \$13,460 for the three months ended March 31, 1998 compared to the three months ended March 31, 1999. This decrease was attributable to capitalized costs of computer software acquired from third party vendors in 1996 that became fully amortized in early 1998.

## FORMER OFFICER'S CONSULTING AND ADMINISTRATIVE EXPENSE

Former officer's consulting and administrative expense remained constant at \$82,680 for the three months ended March 31, 1999 and 1998 respectively. We incurred this expense in connection with our buyout of a former officer's employment agreement in March 1996. At that time the former officer also entered into a covenant not to compete and into a consulting agreement with Pacific Softworks. As of March 31, 1999, the total amount payable to this former officer under these agreements was \$180,000. This sum will be paid in equal monthly installments through September 1999.

YEARS ENDED DECEMBER 31, 1998 AND 1997

## NET REVENUE

Net revenue decreased approximately 16% from 1997 to 1998. Our revenue results primarily from fees for licenses of software products, fees for customer support, training, maintenance and engineering services and royalties. The decrease in revenue for 1998 was attributable primarily to increased competition, related discounting on older product categories, delayed introductions of new products and substantially lower revenue from Japan stemming from recessionary economic conditions in that country.

The increase in international sales from 52% to 58% of total sales for 1997 and 1998 is principally due to a decline in domestic sales as a result of increased competition and related price discounting. We expect international sales to continue to represent a significant portion of net revenue although the percentage may fluctuate from period to period.

We generally price our foreign licenses in dollars. An increase in the relative value of the dollar against Japanese and European currencies may reduce our revenue in dollar terms or could make our products more expensive. As a result, an increase in the relative value of the dollar against other currencies may cause our products to be less competitive in foreign markets. To pay expenses and for other corporate purposes we maintain a small portion of our funds outside of the United States in local currency. We actively monitor our foreign currency exchange exposure and to date this exposure has not had a material impact on the results of operations. To date, we have not utilized derivative instruments to hedge such exposure.

#### COST OF REVENUE

Cost of revenue includes direct and indirect costs for the production and duplication of manuals and media for software products, as well as those relating to packaging, shipping and delivery of the products to our customers. Cost of revenue also includes license and other direct purchase costs of third-party software that we distribute or integrate into our products. Cost of revenue has remained relatively constant for fiscal 1997 and 1998 at approximately 4% of net revenue. As a result, gross profit margins for products have also remained constant at about 96%.

#### SELLING, GENERAL AND ADMINISTRATIVE EXPENSE

Selling, general and administrative expense decreased from \$2,110,038 to \$1,936,117 or 8%, from 1997 to 1998. Because of a 16% decrease in net revenue, these expenses as a percentage of revenue increased from 64% to 69%. The higher absolute expense in 1997 reflected a non-recurring distribution to the president and majority stockholder. Pacific Softworks, then a corporation governed under the provisions of subchapter S of the Internal Revenue Code, made the non-recurring distribution to its president and majority stockholder to permit him to pay corporate income taxes payable for 1996. The decrease in expenditures for 1998 reflected reductions in sales staff and related operating costs in 1998. Our decreases in expenditures were partially offset by increases in corporate consulting expenditures related to strategic planning and marketing and an increase in rent following the relocation of our principal executive offices to our current location in mid 1998.

#### RESEARCH AND DEVELOPMENT EXPENSE

Research and development expense increased from \$834,049 to \$851,568, or 2%, from 1997 to 1998. Because of a 16% decrease in net revenue, research and development expense as a percentage of revenue increased from 25% to 31%. The increase in research and development expense in 1998 was principally attributable to an increase in the number of employees and consultants we hired to assist in the development of the FastTrack(TM) product line and the FUSION WebPilot Micro Browser(TM). These costs were partially offset by a decrease in cost of third-party software acquired for the development process.

## DEPRECIATION AND AMORTIZATION EXPENSE

Depreciation and amortization expense decreased from \$64,195 to \$58,850 or 8%, from 1997 to 1998 and remained constant as a percentage of net revenue at 2%. This decrease in 1998 was attributable to certain capitalized costs of computer software acquired from third party vendors in 1996 that became fully amortized in early 1998.

## FORMER OFFICER'S CONSULTING AND ADMINISTRATIVE EXPENSE

Former officer's consulting and administrative expense remained constant at \$314,286 for 1997 and 1998. This expense increased as a percentage of net revenue from 9% to 11% as a result of the decrease in net revenue. We incurred this expense in connection with our buyout of a former officer's employment agreement in March 1996. At that time, the former officer also entered into a covenant not to compete and into a consulting agreement. Under the consulting agreement, he agreed to make himself available to provide financial consulting to Pacific Softworks as requested. To date, we have not called upon him to render any significant services. As of May 1999, the total amount payable to this former officer under these agreements was approximately \$131,000. This sum will be paid in equal monthly installments through September 1999.

## PROVISION FOR TAXES

Commencing in 1995 we elected to be treated as a subchapter S corporation. Through 1998 all federal tax liabilities were recognized at the individual stockholder level. In February 1999 Pacific Softworks terminated the subchapter S election and became subject to taxation at the corporate level. Our historical financial statements do not reflect any income tax provision or benefit. Had Pacific Softworks been subject to taxation as a C corporation, it would have received pro forma income tax benefits totaling \$48,375 and \$177,750 in 1997 and 1998, based on a combined federal and state tax rate of 37.5%. We will record income tax expense (benefit) in future periods at the corporate level.

## LIQUIDITY AND CAPITAL RESOURCES

At December 31, 1998 and March 31, 1999, we had working capital of \$222,477 and \$546,095 and cash and cash equivalents of \$224,031 and \$460,907. We expect that our cash and financing needs in 1999 will continue to be met by:

- cash on hand,
- cash generated by operations,
- proceeds of \$500,000 from a private sale of securities in February 1999,
- a bank line of credit, and
- net proceeds of this offering.

If these sources of financing are insufficient or unavailable, or if we experience an increase in operating cash requirements, we would slow the rate at which we bring additional FastTrack(TM) products and the FUSION WebPilot Micro Browser(TM) to market. We would also reduce our related marketing and development activities.

To date, we have satisfied operating cash requirements principally through internally generated funds. Our operating activities have generated (used) net cash of \$286,567 and (\$419,480) for 1997 and 1998 and (\$26,286) for the three months ended March 31, 1999. Cash generated by or used in operating activities in each period principally reflected the loss from operations for each period and the related change in working capital components. Decreased revenue for 1998 contributed to decreases in accounts receivable, accounts payable and deferred revenue. Our investing activities during 1998 and the three months ended March 31, 1999 used net cash of \$71,888 and \$27,982 for capital expenditures. Our financing activities during 1998 generated net cash of \$94,500. This net cash primarily resulted from our acquisition of the minority interest in our Japanese subsidiary for \$5,500, that was offset by \$150,000 of short-term borrowings of which \$50,000 was repaid during the period. Our financing activities for the three months ended March 31, 1999 include receipt of \$500,000 from our sale to a single corporate investor of 100,000 shares of common stock. This amount was offset by \$81,541 representing costs incurred through that date in connection with this offering and by a \$100,000 repayment of borrowings.

We have available a \$250,000 bank line of credit, personally guaranteed by our president and majority stockholder, under which no balance was outstanding at December 31, 1998 and March 31, 1999. In 1998 we borrowed \$100,000, interest free, from a company affiliated with our president. Pacific Softworks repaid this loan after December 31, 1998.

#### PRIVATE PLACEMENT

In February 1999 we sold 100,000 shares of restricted common stock to one investor at a price of \$5.00 per share. We also issued 100,000 warrants, allowing the investor to acquire 100,000 shares of common stock at \$6.00 per share. These warrants expire March 1, 2001. We received net proceeds of \$500,000 from this sale.

#### YEAR 2000 ISSUES

We are aware of the issues associated with the programming code in existing computer systems as the year 2000 approaches. The year 2000 problem is pervasive and complex, as many computer systems will be affected in some way by the rollover of the two-digit year value to 00. Systems that do not properly recognize this information could generate erroneous data or cause a system to fail. The year 2000 issue could create risk for us from unforeseen problems in our own computer systems and from third parties with whom we deal on transactions worldwide. Failures of our and/or third parties' computer systems could have a material impact on our ability to conduct business. Based on our review and analysis, however, we believe that our computer systems and software products are year 2000 compliant. We have further concluded that the products we obtain from our vendors and suppliers for use within our systems and products are also year 2000 compliant. We have not incurred and do not expect to incur any material expense in connection with year 2000 matters.

#### INTRODUCTION OF THE EURO

On January 1, 1999, 11 of the 15 member countries of the European Union established fixed conversion rates between their existing sovereign currencies and a new currency called the "Euro." These countries agreed to adopt the Euro as their common legal currency on that date. The Euro trades on currency exchanges and is available for non-cash transactions. The existing sovereign currencies will remain legal tender in these countries until January 1, 2002. On that date the Euro is scheduled to replace the sovereign legal currencies of the member countries.



Our European operations are centered in the United Kingdom, which has not adopted the Euro. We will evaluate the impact the implementation of the Euro will have on our business operations. We do not expect the Euro to have a material effect on our competitive position. We can provide no assurance, however, that the implementation of the Euro will not have a material adverse affect on our business, financial condition and operating results. In addition, we cannot accurately predict the impact the Euro will have on currency exchange rates or our currency exchange risk. We have historically priced our foreign licenses in dollars and as a result we have had no material need to hedge our foreign currency exposure. If competitive conditions require us to license our products in terms of Euro or other currencies, we may engage in currency hedging to manage this exposure in the future if we think that it is appropriate for us to do so.

#### RECENT ACCOUNTING PRONOUNCEMENTS

In June 1997, the Financial Accounting Standards Board, issued Statement of Financial Accounting Standards No. 130. FAS 130 establishes standards for reporting comprehensive income and its components in a financial statement. Comprehensive income as defined includes all changes in equity (net assets) during a period from non-owner sources. Examples of items to be included in comprehensive income, which are excluded from net income, include foreign currency translation adjustments and unrealized gains/losses on available-for-sale securities. We adopted the disclosure prescribed by FAS 130 in fiscal 1997.

In June 1997 Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information." This statement establishes standards for the way companies report information about operating segments in annual financial statements. It also establishes standards for related disclosures about products and services, geographic areas, and major customers. We have not yet determined the impact, if any, of adopting this statement. We will adopt the disclosures prescribed by FAS 131 in the year ending December 31, 1999.

In October 1997 and March 1998 the American Institute of Certified Public Accountants issued Statements of Position 97-2, "Software Revenue Recognition," and 98-4, "Deferral of the Effective Date of a Provision of SOP 97-2, Software Revenue Recognition," which we are currently required to adopt for transactions occurring in the fiscal year beginning January 1, 1998. SOP 97-2 and SOP 98-4 provide guidance on recognizing revenue on software transactions and supersede SOP 91-1. We believe that the adoption of SOP 97-2 and SOP 98-4 will not have a significant impact on our current licensing or revenue recognition practices. However, should we adopt new licensing practices or change our existing licensing practices, our revenue recognition practices may change to comply with the accounting guidance provided in SOP 97-2 and SOP 98-4.

In April 1998 the American Institute of Certified Public Accountants issued Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." SOP 98-1 provides guidance for determining whether computer software is internal-use software as well as guidance on accounting for the proceeds of computer software originally developed or obtained for internal use and then subsequently sold to the public. It also provides guidance on capitalization of the costs incurred for computer software developed or obtained for internal use. We have not yet determined the impact, if any, of adopting this statement. We will adopt the disclosures prescribed by SOP 98-1 in the year ending December 31, 2000.

## WHERE YOU CAN FIND ADDITIONAL INFORMATION

Pacific Softworks has filed with the Securities and Exchange Commission, 450 Fifth Street, Washington, D.C. 20549, a registration statement on Form SB-2 under the Securities Act with respect to the securities offered. This prospectus does not contain all of the information set forth in the registration statement and the exhibits and schedules to the registration statement. For further information concerning Pacific Softworks and the securities offered, we refer you to the registration statement and the exhibits and schedules filed as a part of the registration statement.

Statements contained in this prospectus concerning the contents of any contract or any other document are not necessarily complete. In each instance where a copy of that contract or document has been filed as an exhibit to the registration statement, we refer you to the copy of the contract or document that has been filed. Each statement is qualified in all respects by reference to that exhibit. The registration statement, including its exhibits and schedules, may be inspected without charge at the SEC's principal office in Washington, D.C. and at the SEC's regional offices at Northwest Atrium Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661-2511 and 7 World Trade Center, New York, New York 10048. Copies of all or any part of those documents may be obtained from the SEC's office after payment of the SEC's prescribed fees. The SEC maintains a Web site that contains reports, proxy and information statements and other information regarding companies that file electronically with the SEC at [www.sec.gov](http://www.sec.gov).

We intend to provide our stockholders with annual reports containing consolidated financial statements audited by an independent public accounting firm and quarterly reports containing unaudited consolidated financial data for the first three quarters of each year.

## BUSINESS

## OUR BUSINESS

Pacific Softworks develops and licenses Internet and Web related software and software development tools. Our products enable Internet and Web based communications, based on a set of rules known as protocols, and are embedded into systems and "information appliances" developed or manufactured by others. Information appliances are Internet connected versions of everyday products such as telephones, televisions, fax machines and other digitally based devices.

Rapid advances are enabling wired and wireless information appliances to assume many of the tasks now handled by personal computers. We believe that Web browsing enabled by embedded software in information appliances used by businesses and individuals will be a major market. International Data Corp. estimates that 94% of Internet access is now made through PCs. By 2002, that percentage is expected to decrease to 64%. By 2002 the number of information appliances sold is expected to exceed the number of PCs sold.

We intend to evolve and refine our business to track the growth of embedded software in information appliances that incorporate Internet and Web communications capabilities. As information appliances proliferate, we anticipate that our opportunities for long term revenue growth will also increase.

Our Internet and Web related software development tools offer significant benefits to our customers including:

- accelerated product development and market entry,
- portability across multiple hardware and software system environments, and
- comprehensive embedded solutions that enable information appliances to connect with the Internet and use the Web.

Information appliance manufacturers and software developers have included our products within the following applications and information appliances:

#### Applications

- - - - -

- - Office automation
- - Medical
- - Multimedia
- - Industrial controls
- - Networking
- - Set-top boxes
- - Wireless
- - Navigation systems
- - Defense and aerospace
- - Satellite

#### Information Appliances

- - - - -

- Internet fax, copiers, laser printers, scanners
- Patient monitors, imaging systems
- DVD players, projectors, digital cameras
- Vending machines, traffic controls, scoring systems, security controls
- Routers, switches, network controls, cable modems
- Set-top boxes, Internet TV
- Telephones, personal digital assistants, pagers, electronic organizers
- Navigational controls, air traffic controls
- Engine controls, smart weapons
- Satellite positioning, uplink and downlink of streaming video

We have developed a new proprietary Internet browser for use within independent, "non-Windows(R)" information appliances. We expect to begin marketing this browser, under the "FUSION WebPilot Micro Browser(TM)" name, during the third quarter of 1999. Our browser may be effectively placed in use without an operating system and does not require substantial amounts of memory. We believe that our browser may prove particularly attractive to manufacturers of information appliances who would rather give their products a proprietary or subjective "look and feel" than to be restricted by a browser which requires or depends on the "look and feel" of commercially available operating systems such as Windows(R).

#### OUR STRATEGY

Our objective is to be a leading provider of embedded software that enables information appliances and other devices to connect with and communicate through the Internet and Web. To attain our objective and to increase revenue, we intend to:

- Increase sales and marketing activities,
- Expand our existing collaborative relationships to capitalize on our new micro-browser and other technologies designed for information appliances,
- Create new collaborative relationships with key information appliance manufacturers,
- Maintain research and development of new Internet-based products that enable reliable and secure communication and

transport of data over the Internet, and

- Continue to provide additional functions and features to our existing and upgraded software and communication products.

## BACKGROUND

## INDUSTRY BACKGROUND - SIGNIFICANT GROWTH OF THE INTERNET.

The Internet has grown in less than a decade from a limited research tool to a global network consisting of millions of computers and users. The Internet is expected to continue to grow rapidly. We estimate that the number of Internet users worldwide will grow from approximately 69 million in 1997 to 320 million in 2002. The U.S. Department of Commerce estimates that Internet traffic doubles every 100 days. The number of Internet Web sites is also growing rapidly. The number of Web sites detected by the Netcraft Web Server Survey increased from approximately 526,000 in November 1996 to approximately 1.6 million in November 1997, and to over 3.5 million in November 1998, reflecting annual growth exceeding 100%.

Network Solutions, Inc., which estimates that it holds a 75% worldwide market share in domain name registrations, registered over 1.9 million new domains in 1998, nearly double those of the previous year. The growth of the Internet is primarily attributable to its value as a low-cost, open, and readily accessible platform for communications and commerce.

As a result of these attributes, organizations are increasingly embracing the Internet as a principal platform for communicating with key constituents and conducting business. Internally, many organizations have adopted Internet-based systems to facilitate communications among employees and to automate internal business processes. Many organizations are adding Web-based applications to increase sales, cut costs, and improve customer service. These applications range from Web sites offering electronic brochures, to electronic acquisition of goods and services, and automated customer service and support.

Organizations are making large investments in these applications to create meaningful and attractively presented content that informs, entertains, and communicates. Emerging applications now enable organizations to attract customers and build customer loyalty by offering dynamic, personalized content. Web-based applications for suppliers and distributors have also significantly improved business-to-business procurement, payment systems, and logistics planning. Entirely new businesses have emerged that have been developed specifically to exploit the unique characteristics of the Internet and e-commerce. International Data Corporation forecasts the U.S. Internet Economy to grow for \$124 billion in 1998 to \$518 billion in 2002.

Advertising revenue has also played an important role in the growth of the Internet. Attracted by increasing numbers of users, Internet-based businesses have developed that are supported primarily by advertising revenue. Traditional businesses have also realized incremental advertising spending from their Web sites. We estimate that Internet advertising spending will grow from \$1.9 billion in 1998 to \$7.7 billion in 2002.

## GROWTH OF INTERNET TECHNOLOGY, CONTENT AND INFRASTRUCTURE.

Organizations are supporting their Internet-based systems by investing heavily in technology, content, and infrastructure. Forrester Research estimates that spending on software and services for e-commerce alone will exceed \$5.6 billion in 1998 and \$35 billion by 2002. The creation of Internet content continues to grow rapidly by any measure. For example, as of May 27, 1998, the AltaVista search engine had indexed more than 140 million Web pages, an increase of more than 40 million pages in the first five months of 1998.

The Internet uses Web and specialized servers for different tasks and forms of communications. For example, specialized servers are used for Web browsing, email, chat, news groups, file transfers, and audio and video streaming. A measure of the growth of the Internet infrastructure is the number of Web and other Internet servers that are installed. These servers respond to requests for information and manage data. We estimate that the number of Web and other Internet servers installed will grow from approximately 6.3 million in 1998 to nearly 12 million in the year 2002.

#### OUR SUITE OF PRODUCTS

##### TRANSMISSION CONTROL PROTOCOL/INTERNET PROTOCOL.

Transmission Control Protocol/Internet Protocol, which we refer to below as "TCP/IP," is a suite of communications protocols that have been adopted as a standard and enable the communications that take place on the Internet. As a standard, TCP/IP enables Internet users to adopt or acquire pre-made, "off the shelf" products, such as those of Pacific Softworks, and eliminates the need by those users to develop a proprietary communications infrastructure on their own. The TCP/IP stack is a collection of components consisting of various layers of protocols and programs that operate together to transfer data over the Internet. These protocols include the Internet Protocol, various messaging and addressing protocols, and the Transmission Control Protocol.

Embedded systems consist of a microprocessor and related software incorporated into a product and dedicated to performing a specific set of tasks. The market for embedded Internet applications continues to grow substantially as customers deploy TCP/IP based networks. TCP/IP and related technologies are emerging as the building blocks for next-generation wired and wireless networks. According to Datapro, total industry sales of TCP/IP products is projected to grow at a compounded annual growth rate of 11.6% with industry sales rising from \$1.6 billion in 1995 to \$2.7 billion in 2000.

We believe that key elements defining our market today include the following:

- TCP/IP is a commodity type product that remains a key component of the Internet. Generic public domain software for TCP/IP is available at low cost.
- The competitive market for TCP/IP products currently focuses on selling value-added applications, such as file transfer protocols designed to send large files over the Internet, email, and management tools that enhance the embedded protocol stack.
- The market is migrating away from proprietary protocols to standard Internet protocols.
- Manufacturers continue to implement Internet and Web embedded software in a growing number of consumer and industrial information appliances.
- International market growth will ultimately outpace market growth in the United States.
- As more powerful microprocessors become available and decrease in price, embedded systems are being used in a wider range of applications and are facilitating the development of a new generation of information appliances. Emerging embedded Internet applications for interactive entertainment, network computers, remote management and other uses may offer significant additional opportunities for embedded systems and information appliances.

- Manufacturers of products using embedded technology must bring complex applications for embedded systems to market rapidly and economically. Developing embedded applications has evolved from a relatively modest programming task to a complex engineering effort. As more powerful and affordable 32-bit and 64-bit microprocessors have become available, products based on them have become richer in features and functions.
  
- More sophisticated software solutions are required to develop these more complex applications, frequently including a real-time operating system and Internet and Web products that provide developers with far more features, higher performance and greater productivity than those necessary or feasible for programming prior generations of microprocessors. Our flexible software solutions and powerful development tools allow our customers to create and standardize complex, embedded software applications quickly and efficiently.
  
- As embedded applications increase in complexity, the costs associated with providing software development, support and training of engineers are rising rapidly. In this environment, time-to-market, conformance to standards and product reliability have become critical issues for companies developing information appliances and other devices which may be connected to the Internet.

We have designed FUSION products with the developer in mind. The FUSION solution assists system developers by adding compliant Internet protocols and applications to their products. FUSION products are very flexible and portable. Our products are not dependent on any particular hardware or software. Our products are also designed for easy integration.

Our FastTrack(TM) development products provide a pre-built "drop-in solution" that facilitates quick and easy protocol implementation within the products of our customers. FUSION FastTrack(TM) solutions provide users with a complete suite of networking tools to ease the development and porting of new projects. Our customers do not face the uncertainty of trying to determine what components will work with FUSION. Our engineers have integrated FastTrack(TM) with the processor, operating system, compiler, debugger and development board to assure a simplified and reliable drop-in solution that moves a customer's project to more rapid completion. A user need only add its application and then transfer our software to the targeted hardware or device.

FUSION FastTrack(TM) products are not dependent on any particular processor. They have been and are currently being developed for several families of processors including those of:

- |   |                        |
|---|------------------------|
| - Advanced Micro Devices                      | - LSI Logic            |
| - Advanced Risc Machines                      | - MIPS Technologies    |
| - Analog Devices                              | - Motorola Corporation |
| - ARC   | - NEC                  |
| - Hitachi                                     | - Philips              |
| - Hyperstone                                  | - Siemens              |
| - Intel Corporation                           | - ST Microsystems      |
| - International Business Machines Corporation | - Texas Instruments    |

Our Internet and Web products provide an integrated suite of critical functions which feature:

- a small sized, fast, efficient, high performance embedded Internet protocol stack,
- an extensive range of Internet and Web applications,
- custom-built software code, not based on public domain sources,
- mature software code, tested and used in a wide variety of products by companies including Sony, Motorola, Hewlett-Packard, Intel, IBM, Lucent, Cisco and VLSI,
- code developed for embedded systems and information appliances with fine tuning capabilities built into the code to optimize Internet connectivity for specific applications,
- multiple interface software support for most of the popular communication chip sets, and
- pre-built ready to add "drop-in solutions" for easy integration of customer application software across multiple processor platforms.

## OUR PRODUCTS

### OUR INTERNET AND APPLICATION PRODUCTS

FUSION TCP/IP. This product enables data to be transported over the Internet. Our product is not dependent on any particular processor, operating system or compiler. FUSION is high performance, small, tunable, and can be easily incorporated in a customer's information appliances.

FusOS. This product is our FUSION operating system. Customers may choose to use FusOS or remove it from our Internet product and replace it with any commercial operating system of their choice.

FUSION IPsec. This product is the FUSION IP security protocol suite which provides privacy and authentication services at the Internet Protocol layer. IPsecurity uses advanced encryption algorithm keys and is designed to provide secure financial and e-commerce transactions from information appliances over the Internet.

FUSION Satellite IP. This product adds the power and scalability required for Internet protocols to work in a slow-start or delayed environment such as in satellites and set-top boxes. FUSION Satellite IP is designed to handle communication over satellite links for uplink and downlink modes, and adapts to the delays inherent in satellite communications.

FUSION RIP, Routing Information Protocol. Widely accepted as a standard routing protocol, RIP routers send broadcast messages onto a network and contain routing information about the network. This information is shared among all the RIP-capable routers in a network thereby allowing each router to understand where it exists in a network and where its routes lead. RIP specifies how routers exchange routing table information. Currently, there are industry standards which describe the specifications required to implement RIP. The FUSION RIP protocol is a high-performance portable software engine that implements IP forwarding and route generation consistent with industry standards. With RIP, routers periodically exchange entire tables of routing data. Because this is inefficient, RIP is gradually being replaced by a newer protocol called Open Shortest Path First Protocol, or "OSPF."



FUSION OSPF, Open Shortest Path First Protocol. This product is a portable software engine that fully implements the OSPF to provide routing. It has been designed specifically for use in high performance multi-protocol routers. OSPF defines how routers share routing information. Unlike RIP, which transfers entire tables of routing data, OSPF transfers only routing information which has changed since the previous transfer. As a result, use of this protocol reduces the amount of data to be transmitted and conserves system resources.

FUSION PPP, Point-to-Point Protocol. This product provides a means for transmitting packets of data known as datagrams over serial point-to-point links. This application links one device to another over telephone lines and cable.

FUSION MultiLink PPP. Both FUSION PPP and MultiLink PPP modules may be used in any processor. MultiLink PPP extends PPP over multiple links or channels. MultiLink PPP allows users to broadcast data simultaneously to multiple devices within different operating environments and allows users to transfer more data by combining available links.

FUSION SNMP, Simple Network Management Protocol. SNMP is a set of protocols that interfaces transparently into FUSION TCP/IP. SNMP helps to manage and control devices over the Internet.

FUSION FTP, File Transfer Protocol. This application software allows the efficient sharing of files, programs or data between devices over the Internet. FTP also provides a secure way to allow or deny access to specific files or directories between diverse systems.

FUSION TFTP, Trivial File Transfer Protocol. This product is a subset of FTP that allows the efficient transfer of files between diverse host systems without the extended features and potential overhead associated with FTP. TFTP is designed with small size and easy implementation in mind for devices with minimal memory.

FUSION Telnet. This product is a general, bi-directional oriented communications application which allows a standard method of interfacing or connecting terminal devices and terminal-oriented processes to each other. This application software can be used for terminal-to-terminal and/or application-to-application communications.

FUSION SMTP, Simple Mail Transfer Protocol. This product is a protocol used for sending email messages between servers. SMTP is generally used to send messages from a mail client to a mail server. SMTP is independent of any transmission protocol or operating system and only requires a reliable data stream. We have designed FUSION SMTP to be small, efficient and easy to implement in virtually any environment.

FUSION POP3, Post Office Protocol Version 3. This software provides messaging capability within products or systems that do not have the memory or other resources to use SMTP or where there is no continuous Internet connection. POP3 is typically used to access and retrieve email that is being held on a mail server. Most email applications, sometimes called an email client, use a POP Protocol. POP3 is independent of any transport protocol or operating system and is typically implemented over TCP. We have designed FUSION POP3 to be a small, efficient messaging client that is easy to implement in environments where memory and system resources are sparse.

FUSION BOOTP, Bootstrap Protocol. This is an Internet protocol that enables a diskless device to discover its own IP address, the IP address of a BOOTP server on the network, and a

file to be loaded into memory to activate or boot the device. This application software allows the efficient sharing of files, programs or data between diverse host systems. BOOTP also provides a secure way to allow or deny access to specific files or directories between diverse systems.

FUSION DHCP, Dynamic Host Configuration Protocol. This is a protocol for assigning dynamic addresses to devices on the Internet. With dynamic addressing, a device can have a different address every time it connects to the Internet. DHCP also supports a mix of fixed and dynamic Internet addresses. Dynamic addressing simplifies network administration because the software keeps track of the addresses rather than requiring an administrator to manage the task. This means that a device can be added to the Internet without the difficulties associated with manually assigning it a unique address. Many Internet service providers use dynamic addressing for dial-up users.

#### OUR WEB PRODUCTS

FUSION WebPilot Micro Browser(TM). Our FUSION WebPilot Micro Browser(TM) is a completely embedded browser aimed at applications like set-top boxes, wired and wireless telephones, other hand-held information appliances, kiosks, and other remote Internet information appliances. This application has been designed for limited memory environments and is independent of the operating system, processor or compiler. It is applicable across multiple platforms.

Unlike other browsers based on Windows(R), the FUSION WebPilot Micro Browser(TM) is designed for small space applications. Our browser has also been designed from scratch for embedded applications. Unlike other browsers, the FUSION WebPilot Micro Browser(TM) is not a modified or simplified version of existing PC code. We believe that our product is the only embeddable Web browser that currently can make this claim. Our product provides full browsing capabilities in an embedded environment without needing a full PC-type operating system or Microsoft Windows(R). In addition to browsing capabilities, the FUSION WebPilot Micro Browser(TM) family of products will include email and e-commerce applications in the embedded environment.

The FUSION WebPilot Micro Browser(TM) has its own embedded windowing and graphical support. These features allow users to create custom designs and custom fonts and icons. We believe that these features are particularly important in addressing foreign languages such as Japanese and in developing branded presentation screens for customers.

We have designed the FUSION WebPilot Micro Browser(TM) to permit incorporation of various add-on modules. Our browser will have a functionality and presentation similar to those of the much larger PC-based browsers such as Internet Explorer and Netscape but will have substantially reduced memory requirements. We intend actively to market and deliver FUSION WebPilot Micro Browser(TM) during the third quarter of 1999.

FUSION Embedded Web Server. This application software allows any user on the Internet easily to manage or monitor any device connected to the Internet. It provides an easy way to deliver powerful Web-based applications in generally understood graphical formats. Using FUSION Internet protocols, FUSION Web Server provides integrated Web services. It provides Web servers with the capability to look at and manage any Internet connected devices through the Web. Examples of such uses include:

- video cameras,
- vending machines,

- utility power meters,
- medical equipment, and
- other remote devices.

The FUSION Web Server is compatible with FUSION WebPilot Micro Browser(TM) and all other standard browsers including Netscape, Mosaic, and Internet Explorer, on all platforms. We intend actively to market and deliver FUSION Web Server during the third quarter of 1999.

#### OTHER PRODUCTS WE INTEND TO MARKET

FUSION 6. This product is our major TCP/IP upgrade. We are designing this application to provide greater security and flexibility in connection with the next generation Internet Protocol. We expect to introduce this product within the next 12-18 months.

FUSION Mobile IP. We are designing this product for use within wireless and cellular applications. Internet protocols do not currently operate efficiently in wireless environments. We are designing Mobile IP to handle information processing delays and interruptions associated with Internet protocols in wireless applications. We expect to introduce this product within the next 12-18 months.

#### SERVICES AND SUPPORT

Pacific Softworks seeks to provide comprehensive customer service and support which help customers realize the value and potential of our products.

#### TRAINING CLASSES

We offer several training courses and workshops for an additional fee. We provide courses monthly at our executive office in California or in the United Kingdom. We also provide training courses at customer sites. We tailor these training courses to meet specific customer needs and schedules.

#### TECHNICAL SUPPORT

Our technical support staff assists customers with problems and questions in the installation and use of our products. We bundle technical support with product updates and maintenance on an annual fee basis.

#### ENGINEERING SERVICES.

We provide a number of services on a fee-for-service basis, including application-level consulting, customization, and porting to proprietary semiconductor architectures. We coordinate and perform these services in North America, Japan and Europe.

#### INDUSTRY COLLABORATION

Pacific Softworks works with various companies in jointly developing products for the Internet market for those companies and their customers. The nature of this work is generally a process of informal collaboration that does not require written agreements or ongoing legal

obligations. We have described some of our more significant collaborations below. We plan to continue developing these and other relationships.

**INTEL.** Under a program called "wired for manageability," Intel has worked with Pacific Softworks and has incorporated FUSION Internet software products into various Intel products.

**MOTOROLA.** Pacific Softworks and Motorola have collaborated for a number of years on providing Internet connectivity for most of the Motorola product families. Pacific Softworks has provided Internet solutions for Motorola customers. In return members of the Motorola sales force and application engineers have recommended Pacific Softworks as a solution partner to their customers.

**ST MICROELECTRONICS.** ST Microelectronics has worked with Pacific Softworks in the United States and Europe on incorporating our products with the set-top boxes, cable modems and other product designs of ST Microelectronics.

**ADVANCED RISC MACHINES.** Advanced RISC Machines and Pacific Softworks have worked together to incorporate FUSION products onto the ARM7 development board, a foundation used for the development of other products. ARM recommends Pacific Softworks products to its customers.

**TEXAS INSTRUMENTS.** Since late 1998 Texas Instruments has been evaluating the FUSION Protocols on its set-top box development board. We are currently discussing joint development for new Texas Instruments products. In addition, FUSION Internet protocols have been incorporated into digital signal processors of Texas Instruments.

**ANALOG DEVICES INC.** Analog has licensed both our browser and our email technology for use in conjunction with its SHARC chip set. The license is royalty bearing. These digital signal processors are targeted at a variety of communications applications including digital television and video phones. Our software will be bundled with the chip set that will also form part of Analog's SHARC development platform design. We expect to work with Analog to meet the requirements of its customers worldwide and to work on joint developments for the next generation of information appliance technology.

#### TOOLS AND OPERATING SYSTEM COLLABORATION

We currently work or collaborate with the following companies in developing and expanding our FastTrack(TM) suite of products:

**GREENHILLS SOFTWARE.** Several of our FastTrack(TM) developer kits are based on GreenHills' tools suite. These products provide a strong development environment and are well accepted in the embedded market.

**EXPRESS LOGIC.** We have worked with Express Logic for about two years. We believe that Express Logic has superior real-time operating systems products for the embedded market. Most of our FastTrack(TM) solutions are built using this real-time operating system. In addition, with the exception of Germany and Switzerland, Pacific Softworks distributes Express Logic software code on a non-exclusive basis worldwide.

DIAB DATA CORPORATION. Pacific Softworks has worked with Diab Data for over three years on Motorola platforms. Diab Data is a leading supplier of software tools for Motorola based products.

SOFTWARE DEVELOPMENT SYSTEMS. Pacific Softworks has collaborated with Software Development Systems to use the Software Development Systems compiler for Motorola platforms. Based on informational available to us, we believe that Software Development Systems has over 50% of compiler sales for Motorola products.

GAIO JAPAN. GAIO is the largest supplier of integrated tools in Japan. We are currently building our Hitachi FastTrack(TM) products with the complete tools suite from GAIO. In return we believe we have become the Internet software supplier of choice for GAIO.

#### WIDE AREA NETWORK COLLABORATION

TELENETWORKS. Telenetworks and Pacific Softworks have recently co-developed a complete router reference platform with Motorola for the small office/home office market. This router reference platform is being reviewed by 3COM and other companies. The collaboration is continuing for other wide area network products. Pacific Softworks is a worldwide value added reseller for Telenetworks. The combination of our products with those of Telenetworks provides a complete WAN/LAN solution for the products manufactured by our customers.

UNISOFT JAPAN. Unisoft is experienced in developing and integrating Internet and Web protocols for customer applications. In addition it provides wide area network solutions for the Japanese market. Pacific Softworks and Unisoft have cooperated on several joint developments involving our FUSION WebPilot Micro Browser(TM) within automobile navigation systems.

#### CUSTOMERS

Since incorporation in 1992, Pacific Softworks has licensed its products to over 400 companies around the world, including: Alcatel, AT&T, America OnLine, Canon, Canal+, Cisco, Cocom, Bell Labs, Data General, Concurrent Technologies, Ericsson, General Instruments, Hughes, Honeywell, Hewlett Packard, Intel, Motorola, Newbridge, Nortel, Psion, Philips, Samsung, Siemens, ST Microsystems, Tandberg, Unisys, and VLSI.

No single customer accounted for more than 10% of our total revenue in 1997 or 1998.

#### MARKETING, SALES AND DISTRIBUTION

In North America, Europe and Japan, we market our products and services primarily through our own direct sales organization, which consists of salespersons and field application engineers. As of December 31, 1998, Pacific Softworks had four domestic salespersons and field application engineers located in North America, one salesperson and field application engineer in Europe and three sales and marketing employees in Japan.

We distribute our products in Japan through a wholly owned subsidiary, Network Research Corporation Japan. We have licensed our products exclusively to Network Research for distribution in Japan.

We have appointed international distributors to serve customers in regions not serviced by our direct sales force. We also collaborate with semiconductor and software vendors and work

closely with a number of system integrators worldwide. These relationships enable us further to broaden the geographic and market scope for our products.

Revenue from international sales represented approximately 52% and 58% of our total revenue in fiscal 1997 and 1998. Revenue from international sales represented approximately 57% of our total revenue for the three months ended March 31, 1998.

Pacific Softworks has experienced, and expects to continue to experience, significant seasonality of revenue resulting primarily from customer buying patterns and product development cycles. We have generally experienced the strongest demand for our products in the fourth quarter of each fiscal year and the weakest demand in the first quarter of each fiscal year. Quarterly revenue typically decreased in the first quarter of each fiscal year from the fourth quarter of the prior fiscal year.

#### COMPETITION

The embedded Internet and Web-based software industry is highly competitive and is characterized by rapidly advancing technology. We believe that we compete favorably in our markets on the basis of:

- product capabilities,
- price/performance characteristics,
- product portability,
- ease of use, and
- support services and corporate reputation.

We compete with other independent software vendors, including Wind River Systems, Inc., Integrated Systems, Inc., Mentor Graphics, Inc. (through its acquisition of Microtec/Ready Systems), Microware Systems Corporation and Microsoft Corporation. In addition, hardware or other software vendors could seek to expand their product offerings by designing and selling products that directly compete with or adversely affect sales of our products.

Many of our existing and potential competitors have substantially greater financial, technical, marketing and sales resources than we have. We are aware of ongoing efforts by competitors to emulate the performance and features of our products and we can provide no assurance that competitors will not develop equivalent or superior technology to that of Pacific Softworks.

Because we have been substantially dependent on our TCP/IP family of Internet products and services, the effects of competition could be more adverse on us than would be the case if we had a broader product offering. In addition, competitive pressures could cause us to reduce the prices of our products, which would result in reduced profit margins. We cannot assure you that we will be able to compete effectively against our current and future competitors. If we are unable to compete successfully, our business, financial condition and operating results would be materially adversely affected.

## PRODUCT DEVELOPMENT AND ENGINEERING

The embedded software industry faces a fragmented market characterized by ongoing technological developments, evolving industry standards and rapid changes in customer requirements. We believe that our success will depend in large part on our ability to:

- maintain and enhance our current product line,
- develop and introduce in a timely manner new products that take advantage of technological advances,
- identify and implement emerging standards,
- offer products across a spectrum of microprocessor families used in the embedded systems market, and
- support sustained marketing and promotion of brand identity and product lines.

During 1997 and 1998 we incurred product development and engineering expenses of \$834,049 and \$851,568. We intend to increase our commitment to product development and engineering for 1999 from the proceeds of this offering.

Pacific Softworks has from time to time experienced delays in the development of new products and the enhancement of existing products. These delays are commonplace in the software industry. We cannot assure you that we will be successful in developing and marketing, on a timely basis or at all, competitive products, product enhancements and new products that respond to technological change, and changes in customer requirements. We also cannot assure you that our enhanced or new products will adequately address the changing needs of the marketplace. The inability of Pacific Softworks, due to resource constraints or technological or other reasons, to develop and introduce new products or product enhancements in a timely manner could have a material adverse effect on our business, financial condition or operating results.

From time to time, we or our competitors may announce new products, capabilities or technologies that have the potential to replace or shorten the life cycles of our existing products. We cannot assure you that announcements of currently planned or other new products by us or others will not cause customers to defer purchasing existing products. Any failure by Pacific Softworks to anticipate or respond adequately to changing market conditions, or any significant delays in product development or introduction, could have a material adverse effect on our business, financial condition and operating results.

As a result of their complexity, software products may contain undetected errors or compatibility issues, particularly when first introduced or as new versions are released. Despite testing by us and testing and use by current and potential customers, it is always possible for errors to be found in new products after shipments to our customers. The occurrence of these errors could result in loss of or delay in market acceptance of our products, which could have a material adverse effect on our business, financial condition and operating results.

Our products are increasingly used for applications in systems that interact directly with the general public, particularly applications in transportation, medical systems and other markets where the failure of the embedded system could cause substantial property damage or personal injury. This failure of our products could expose Pacific Softworks to significant product liability claims. In addition, our products may be used for applications in mission-critical business systems where the failure of the embedded system could be linked to substantial economic loss.

Although Pacific Softworks has not experienced any product liability or economic loss claims to date, the sale and support of our products entail the risk of these claims.

#### PROPRIETARY RIGHTS

Our success is heavily dependent upon our proprietary technology. We rely on a combination of:

- copyright,
- trade secret and trademark laws,
- nondisclosure,
- other contractual restrictions on copying, or distribution, and
- technical measures to protect our software, documentation and other written materials.

As a part of our confidentiality procedures, we generally enter into nondisclosure agreements with our employees and consultants and limit access to and distribution of our software, documentation and other proprietary information. End user licenses of our software are frequently in the form of source license agreements, which are signed by licensees, and which we believe may be enforceable under the laws of many jurisdictions.

Despite our efforts to protect our proprietary rights, unauthorized third parties may be able to copy our products or to reverse engineer or obtain and use information that we regard as proprietary. We can provide you with no assurance that competitors will not independently develop technologies that are substantially equivalent or superior to ours. Policing unauthorized use of our products is difficult. We are unable to determine the extent to which software piracy of our products exists. Software piracy, however, can be expected to be a continuing and persistent problem.

We believe that, due to the rapid pace of innovation within our industry, factors such as the technological and creative skills of our personnel are more important to establishing and maintaining a technology leadership position within the industry than are the various legal protections of our technology.

As the number of patents, copyrights, trademarks, trade secrets and other intellectual property rights in our industry increases, products based on our technology may increasingly become the subject of infringement claims. We can provide you with no assurance that third parties will not assert infringement claims against us in the future. Any of these claims with or without merit could:

- be time consuming,
- result in costly litigation,
- cause product shipment delays, or
- require us to enter into unwanted royalty or licensing agreements.



These royalty or licensing agreements, if required, may not be available on terms acceptable to us, or at all, which could have a material adverse effect on our business, financial condition and operating results.

In addition, we may initiate claims or litigation against third parties for infringement of our proprietary rights or to establish the validity of our proprietary rights. Litigation to determine the validity of any claims, whether or not such litigation is determined in favor of Pacific Softworks, could result in significant expense to Pacific Softworks and divert the efforts of our technical and management personnel from productive tasks. The outcome or settlement of any such litigation may require us to:

- pay substantial damages,
- discontinue the use and sale of infringing products,
- expend significant resources to develop non-infringing technology, or
- obtain a license to the infringing technology.

Any of these events could have a material adverse effect on our business financial condition and operating results.

#### MANUFACTURING AND BACKLOG

Our manufacturing operation consists of assembling, packaging and shipping the software products and documentation needed to fulfill each order. We manufacture our source code for sale and duplicate compact disks in our California facility. We use outside vendors to print documentation and manufacture packaging materials. We believe that backlog is not a meaningful indicator of revenue that can be expected in future periods.

#### EMPLOYEES

As of May 1, 1999, Pacific Softworks employed 27 persons full-time, including four in sales and marketing, 20 in product development, engineering and support and three in management, operations, finance and administration. Of these employees, 24 are located in North America, two are located in Japan and one is located in Europe. None of our employees is represented by a labor union or is subject to a collective bargaining agreement. We have never experienced a work stoppage. We believe that relations with our employees are good.

#### PROPERTIES

Our executive offices are located in a leased facility in Newbury Park, California consisting of approximately 11,500 square feet of office space. The lease for this facility expires in September 2000. Our monthly lease payment is approximately \$8,500. In Japan we have subleased space of approximately 700 square feet at a rate of approximately \$1,600 on a month to month basis. We believe that these facilities are adequate for our current needs and for expected personnel additions over the next 18 months. In the United Kingdom our representative operates from facilities that are secured by him and which entail no material ongoing obligation by Pacific Softworks.

#### LEGAL PROCEEDINGS

We are not a party to any material legal proceedings.

## MANAGEMENT

## DIRECTORS AND EXECUTIVE OFFICERS

The directors and executive officers of Pacific Softworks are:

Name	Age	Position
- - - - -	---	-----
Glenn P. Russell	44	Chairman, President, and Chief Executive Officer
William E. Sliney	60	Chief Financial Officer
Chaim Kaltgrad	45	Vice President - Program Management
Mark Sewell	37	Vice President - Business Development
Sandra J. Garcia	37	Vice President - North American Sales
Robert G. J. Burg II	42	Director
Wayne T. Grau	49	Director
Reuben Sandler, Ph.D.	62	Director
Joseph Lechman	32	Secretary

Glenn P. Russell. Mr. Russell has been our chairman, president and chief executive officer since 1992. Before 1992 he had various sales and marketing positions at IBM, Unisys and Network Research Corporation, a predecessor of Pacific Softworks. Mr. Russell is also an officer and director of Luke Systems International, a distributor of electronic components. Luke Systems International is controlled by Mr. Russell's spouse. Mr. Russell devotes substantially all of his time to Pacific Softworks. Mr. Russell was educated in and is a native of the United Kingdom.

William E. Sliney. Mr. Sliney has been our chief financial officer since April 1999. Before joining us, Mr. Sliney was the chief financial officer for Legacy Software Inc. from 1995 to 1998. From 1993 to 1994, Mr. Sliney was chief executive officer for Gumps. Mr. Sliney received his masters in business administration from the University of California at Los Angeles.

Chaim Kaltgrad. Mr. Kaltgrad has been our vice president - program management since May of 1999. From 1992 to 1999, Mr. Kaltgrad was a consultant for Lockheed Martin Corporation. From 1997 to 1998 Mr. Kaltgrad was also a consultant at Demo Systems. He received a masters degree in computer science from California State University Northridge and a bachelors of mathematics and computer science from the University of California at Los Angeles.

Mark Sewell. Mr. Sewell, a resident of the United Kingdom, has been the general manager for our European operations since 1996, with responsibility for European sales and business development. For over two years prior to 1996, he was the business and support manager for the Asia Pacific region of PictureTel, Inc. He received his masters degree in electrical and electronic engineering from the University of Canterbury.

Sandra J. Garcia. Ms. Garcia joined us in 1993 as our regional sales manager and became vice president - North American sales in 1996. Ms. Garcia graduated from Santa Barbara College.

Robert G. J. Burg II. Mr. Burg has been a director of Pacific Softworks since January 1999. He has been the president of Profile Sports, a corporate sports and outing entertainment business, since 1998. For more than five years before that he served as president, senior vice president and in other managerial positions at Royal Grip, Inc., a manufacturer and distributor of golf grips and sports headwear. Mr. Burg received a bachelor of arts degree from the University

of Colorado. He currently serves on the boards of directors of EMD/Empyean Diagnostics, Ltd. and Royal Precision, Inc.

Wayne T. Grau. Mr. Grau has been a director of Pacific Softworks since January 1999. He has been the president and chief executive officer of Fielding Electric, Inc. since 1981. He is currently a member of the Los Angeles Chapter membership committee of the National Electrical Contractors Association, a trustee for the Joint Apprenticeship Training Committee and a trustee for the Los Angeles Electrical Training Trust.

Reuben Sandler, Ph.D. Dr. Sandler has been a director of Pacific Softworks since January 1999. He has been the president and chief information officer for MediVox, Inc., a medical software development company, since June 1997. From 1989 to 1996, he was an executive vice president for R&D Laboratories, Inc. Dr. Sandler received a Ph.D. from the University of Chicago and is the author of four books on mathematics. He currently serves on the boards of directors of MediVox, Inc. and Alliance Medical Corporation and is an advisor to the board of directors of R&D Laboratories, Inc.

Joseph Lechman. Mr. Lechman has been our secretary since March 1999. He is a principal in the law firm of Gose & Lechman and has been practicing law in Ventura County, California since 1991. Mr. Lechman received his bachelor of arts degree in business administration in 1987 from California State University at Fullerton. He received his juris doctorate from Pepperdine University School of Law and was admitted to the State Bar of California in 1990. Mr. Lechman obtained a master's of law in taxation from the New York University School of Law.

#### BOARD OF DIRECTORS

Our directors are elected for a one year term. Each director holds office until the expiration of his term, until his successor has been duly elected and qualified or until the earlier of his resignation, removal or death. Each officer serves at the discretion of the board of directors. There are no family relationships among any of our directors or officers.

Our directors receive \$200 for attending meetings of the board of directors. We will also reimburse our directors for actual and reasonable out of pocket expenses incurred when attending board of directors and committee meetings. Directors who are not employees are eligible to participate in the 1998 Equity Incentive Program. Each of our non-employee directors received options to purchase 15,000 shares of common stock upon his election to the board of directors.

#### COMMITTEES OF THE BOARD OF DIRECTORS

The board of directors maintains a compensation committee and an audit committee. The compensation committee is composed of Reuben Sandler, chair, Robert Burg and Wayne Grau. The audit committee is composed of Robert Burg, chair, Reuben Sandler and Wayne Grau. The compensation committee reviews and makes recommendations to the board of directors on compensation matters, including bonuses, of our officers and administers the grants under our equity incentive program. The audit committee:

- reviews the scope of the audit procedures employed by our independent auditors,
- reviews our accounting practices and policies with our independent auditors,
- recommends to whom reports should be submitted within Pacific Softworks,
- reviews with the independent auditors their final audit reports,

- reviews our overall accounting and financial controls with our internal and independent auditors,
- has its members available to the independent auditors for consultation,
- approves the audit fee charged by the independent auditors,
- reports to the board of directors with respect to the matters described above, and
- recommends the selection of the independent auditors.

## EXECUTIVE COMPENSATION

The following table sets forth the compensation earned by our chief executive officer, senior vice president, and vice president for services, or the named executive officers, rendered during the fiscal years ended December 31, 1998, 1997 and 1996. No other executive officer of Pacific Softworks earned or was paid compensation of more than \$100,000 in the year ended December 31, 1998.

## SUMMARY COMPENSATION TABLE

Name and Principal Position - - - - -	Year ended Dec. 31 -----	Salary -----	Annual Compensation Bonus -----	Other -----
Glenn P. Russell Chairman, President, Chief Executive Officer and Chief Financial Officer	1998	\$ 207,962	\$ --	\$ --
	1997	215,384	118,201	--
	1996	162,501	--	--
Mark Sewell Vice President - Business Development	1998	134,822	--	262,500
	1997	115,885	--	--
	1996	58,161	--	--
Sandra J. Garcia Vice President - North American Sales	1998	120,442	--	262,500
	1997	154,563	--	--
	1996	175,750	--	--

Pacific Softworks paid Glenn P. Russell \$118,201 in 1997 in addition to his salary to permit Mr. Russell to pay 1996 personal tax obligations arising from Pacific Softworks' S corporation status. In February 1999 Pacific Softworks terminated the subchapter S election and became subject to taxation at the corporate level.

In June 1998 Pacific Softworks granted to each of Mark Sewell and Sandra J. Garcia options to purchase 70,000 shares of common stock. The calculations of the value of the unexercised options reflected in the above table under "Other" are based on the difference between the fair market value per share of the common stock on December 31, 1998, approximately \$5.00, and the exercise price of each option multiplied by the number of shares covered by the option.

## OPTION GRANTS IN 1998

The following table sets forth each grant of stock options to named executive officers during the fiscal year ended December 31, 1998.

## OPTION GRANTS FOR FISCAL YEAR ENDED DECEMBER 31, 1998

Name	Number Of Securities Underlying Options/SARs Granted	Percent Of Total Options/SARs Granted to Employees in Fiscal Year 1998	Exercise Price	Expiration Date
Mark Sewell	70,000	50%	\$1.25	June 25, 2008
Sandra J. Garcia	70,000	50%	\$1.25	June 25, 2008

These options were not granted under, and are separate from, our equity incentive program. The options may be exercised at any time during their term. There were no options exercised in fiscal year 1998.

## EQUITY INCENTIVE PROGRAM

Our 1998 equity incentive program was adopted by the board of directors and approved by stockholders in April 1998. The number of shares of common stock reserved for issuance under the equity incentive program is 320,000 shares. As of December 31, 1998, no options were granted under the equity incentive program.

Under the equity incentive program, employees, non-employee members of the board and consultants may be awarded options to purchase shares of common stock, stock appreciation rights, restricted shares or stock units. Options may be incentive stock options designed to satisfy the requirements of Section 422 of the Internal Revenue Code of 1986, or nonstatutory stock options designed not to meet those requirements. If restricted shares or shares issued upon the exercise of options granted under this plan are forfeited, then these shares will again become available for awards under the equity incentive program. If stock units, options or stock appreciation rights granted under the equity incentive program are forfeited or terminate for any other reason before being exercised, then the corresponding shares will again become available for awards under the equity incentive program.

The equity incentive program is administered by the compensation committee of the board of directors. This committee has complete discretion to:

- determine who should receive any award,
- determine type, number, vesting requirements and other features and conditions of an award,
- interpret the equity incentive program, and
- make all other decisions relating to the operation of the equity incentive program.

The exercise price for statutory and incentive stock options granted under the equity incentive program may not be less than 85% or 100%, respectively, of the fair market value of the common stock on the option grant date and may be paid in cash or in outstanding shares of

common stock. Holders may exercise options by using a cashless exercise method, a pledge of shares to a broker or promissory note. The payment for an award of newly issued restricted shares will be made in cash, by promissory note or the rendering of services.

The committee has the authority to modify or extend outstanding options and stock appreciation rights. The committee may also accept the cancellation of outstanding options or stock appreciation rights in return for a grant of new options or stock appreciation rights for the same or a different number of shares at the same or a different exercise price.

If there is a change in control of Pacific Softworks, an award will become fully exercisable as to all shares subject to an award if the award is not assumed by the surviving corporation or its parent and the surviving corporation or its parent does not substitute such award with another award of substantially the same terms. In the event of an involuntary termination of service within 18 months following a change in control, all of the awards then outstanding and not vested will then be fully vested.

A change in control includes:

- a merger or consolidation of Pacific Softworks after which our then current stockholders own less than 50% of the surviving corporation,
- sale of all or substantially all of the assets of Pacific Softworks,
- a proxy contest that results in replacement of more than one-third of the directors over a 24-month period, or
- acquisition of 50% or more of our outstanding stock by a person other than a trustee of our equity incentive program or a corporation owned by the stockholders of Pacific Softworks in substantially the same proportions as their stock ownership in Pacific Softworks.

In the event of a merger or other reorganization, outstanding options, stock appreciation rights, restricted shares and stock units will be subject to the agreement of merger or reorganization, which may provide for:

- the assumption of outstanding awards by the surviving corporation or its parent,
- their continuation by Pacific Softworks (if Pacific Softworks is the surviving corporation),
- accelerated vesting, and
- for settlement in cash followed by cancellation of outstanding awards.

The board of directors may amend or terminate the equity incentive program at any time. Amendments may be subject to stockholder approval to the extent required by applicable laws. The equity incentive program will continue in effect unless otherwise terminated by the board of directors.

In May 1999 the board of directors voted to grant our officers and other employees options to purchase 320,000 shares of common stock under our equity incentive plan at an exercise price of \$5.00 per share. These options have a term of 10 years but vest at the rate of 2% per month from the date of grant over a period of 36 months and may not be exercised until after 30 days from the date of this offering.

The table below sets forth grants of options in May 1999 under our equity incentive plan to our named officers:



## OPTION GRANTS IN MAY 1999 UNDER OUR EQUITY INCENTIVE PLAN

Name ----	Number of Options Granted -----	Percent of Total Options Granted to Employees in 1999 -----	Exercise Price -----	Expiration Date -----
Glenn P. Russell	30,000	9.375%	\$5.00	April 30, 2009
William E. Sliney	12,000	3.75%	\$5.00	April 30, 2009
Chaim Kaltgrad	12,000	3.75%	\$5.00	April 30, 2009
Mark Sewell	12,000	3.75%	\$5.00	April 30, 2009
Sandra J. Garcia	12,000	3.75%	\$5.00	April 30, 2009
Joseph Lechman	12,000	3.75%	\$5.00	April 30, 2009

Following the option grants in May 1999 all shares of common stock reserved for issuance under our 1998 equity incentive program have been granted. No additional options will be available under the equity incentive program except to the extent that currently issued options do not vest or are forfeited.



## CERTAIN TRANSACTIONS

## SHARE PURCHASE AGREEMENT - MINORITY STOCKHOLDER

In March 1996, Pacific Softworks agreed with a former officer, director and principal stockholder to a buyout of his employment agreement and Glenn P. Russell agreed to purchase all of that former officer's shares of common stock of Pacific Softworks. Pacific Softworks and that former officer also entered into a consulting agreement and that former officer agreed not to compete with Pacific Softworks. Pacific Softworks paid the former officer \$314,286 for each of 1997 and 1998. As of May 1999 the balance of our payments due to this former officer under these agreements is approximately \$131,000. This amount is payable in equal monthly installments through September 1999. Our agreement with this former stockholder restricts us from making any distributions to stockholders, other than those necessary for tax liabilities resulting from corporate earnings during the time we were an S corporation. Our obligations to the former stockholder are secured by substantially all of the outstanding shares of common stock of Pacific Softworks owned by Glenn P. Russell and all assets of Pacific Softworks.

## TRANSACTIONS WITH AFFILIATE

## LOAN FROM AFFILIATE

In December 1998, Luke Systems International, a company controlled by the spouse of Glenn P. Russell, loaned Pacific Softworks \$100,000 interest free. In March 1999, Pacific Softworks repaid the loan.

## RENTAL OF PREMISES TO AFFILIATE

We rent a portion of our premises to a company affiliated with our chief executive officer. We believe the terms of occupancy to be favorable to us. We expect this affiliated company to relocate to other premises in or around the middle of 1999.

Pacific Softworks believes that the transactions set forth above were made on terms no less favorable to Pacific Softworks than could have been obtained from unaffiliated third parties. All future related party transactions will be approved by a majority of the board of directors, including a majority of the independent and disinterested outside directors on the board of directors, and will be made on terms no less favorable to Pacific Softworks than could be obtained from unaffiliated third parties.

## INDEMNIFICATION

Our articles of incorporation limit the liability of our directors for monetary damages arising from a breach of their fiduciary duty as directors, except to the extent otherwise required by the California General Corporation Law. This limitation of liability does not affect the availability of equitable remedies such as injunctive relief or rescission.

Our bylaws require us to indemnify our directors and officers to the fullest extent permitted by California law, including in circumstances in which indemnification is otherwise discretionary under California law. We have also entered into indemnification agreements with our officers and directors containing provisions that may require us, among other things, to indemnify these officers and directors against certain liabilities that may arise by reason of their status or service

as directors or officers (other than liabilities arising from willful misconduct of a culpable nature), to advance their expenses incurred as a result of any proceeding against them as to which they could be indemnified, and to obtain directors' and officers' insurance if available on reasonable terms.

Insofar as indemnification for liabilities arising under the Securities Act, may be permitted to directors, officers and control persons of Pacific Softworks under the provisions described above, or otherwise, Pacific Softworks has been advised that in the opinion of the SEC, this indemnification is against public policy as expressed in the Securities Act, and is unenforceable.

#### PRINCIPAL STOCKHOLDERS

The following table sets forth certain information regarding beneficial ownership of our common stock as of the date of this prospectus, and as adjusted to reflect the sale of the units offered by this prospectus, by:

- each person who is known by Pacific Softworks to own beneficially more than 5% of our outstanding common stock,
- each of our executive officers and directors, and
- all executive officers and directors as a group.

Shares of common stock not outstanding but deemed beneficially owned because an individual has the right to acquire the shares of common stock within 60 days are treated as outstanding when determining the amount and percentage of common stock owned by that individual and by all directors and executive officers as a group. Each person has sole voting and investment power with respect to the shares of common stock shown. The address of each person is 703 Rancho Conejo Boulevard, Newbury Park, California 91320.

Name and Address of Beneficial Owner -----	Number of Shares Beneficially Owned -----	Percentage of Shares Outstanding -----	
		Before Offering -----	After Offering -----
Glenn P. Russell .....	3,000,000	90.91%	73.17%
William E. Sliney .....	*	*	*
Chaim Kaltgrad .....	*	*	*
Mark Sewell .....	70,000	2.08	1.68
Sandra J. Garcia .....	70,000	2.08	1.68
Robert G. J. Burg II .....	15,000	*	*
Wayne T. Grau .....	15,000	*	*
Reuben Sandler, Ph.D .....	15,000	*	*
Joseph Lechman .....	*	*	*
All directors and executive officers as a group (9 persons) .	3,185,000	91.39%	74.33%

The table above includes shares of common stock issuable upon exercise of options granted to two officers and to each of our three non-employee directors. The table above does not reflect options for the purchase of 30,000 shares of common stock granted in May 1999 to Glenn P. Russell. The table above also does not reflect options for the purchase of 12,000 shares of common stock granted in May 1999 to each of William E. Sliney, Chaim Kaltgrad, Mark Sewell, Sandra J. Garcia and Joseph Lechman. Asterisks in the above table indicate beneficial ownership of less than 1%.

## DESCRIPTION OF SECURITIES

The authorized capital stock of Pacific Softworks consists of 50,000,000 shares of \$0.001 par value common stock and 10,000,000 shares of \$0.01 par value preferred stock, which Pacific Softworks may issue in one or more series as determined by the board of directors. There currently are 3,300,000 shares of common stock issued and outstanding that are held of record by three stockholders.

## UNITS

Each unit being offered in this prospectus consists of one share of common stock and one warrant. The common stock and warrants are separately transferable. There is currently no trading market for the common stock or warrants of Pacific Softworks, and we can provide no assurance that a trading market will develop in the future.

## PREFERRED STOCK

Our board of directors is authorized to issue from time to time, without stockholder authorization, in one or more designated series, any or all of the authorized but unissued shares of preferred stock with such dividend, redemption, conversion, and exchange provisions as may be provided by the board of directors with regard to such particular series. Any series of preferred stock may possess voting, dividend, liquidation, and redemption rights superior to those of the common stock.

The rights of the holders of common stock will be subject to and may be adversely affected by the rights of the holders of any preferred stock that may be issued in the future. Issuance of a new series of preferred stock could make it more difficult for a third party to acquire, or discourage a third party from acquiring, the outstanding shares of common stock of Pacific Softworks and make removal of the board of directors more difficult. No shares of preferred stock are currently issued and outstanding, and Pacific Softworks has no present plans to issue any shares of preferred stock.

## COMMON STOCK

Each holder of record of common stock is entitled to one vote for each share held on all matters properly submitted to the stockholders for their vote. Before election of directors, any stockholder may cumulate votes for any candidate, if a stockholder has given notice that he intends to cumulate his votes and if the candidate's name was placed in nomination prior to voting. In cumulative voting, each stockholder is entitled in the election of directors to one vote for each voting share held by him multiplied by the number of directors to be elected. Each stockholder may cast all of those votes for a single nominee for director or he may distribute those votes among any two or more nominees as the stockholder deems appropriate.

Holders of outstanding shares of common stock are entitled to those dividends declared by the board of directors out of legally available funds and, in the event of liquidation, dissolution or winding up of the affairs of Pacific Softworks, holders are entitled to receive, pro rata, the net assets of Pacific Softworks available to the common stockholders. Holders of outstanding

common stock have no preemptive, conversion or redemption rights. All of the issued and outstanding shares of common stock are, and all unissued shares of common stock, when offered and sold will be, duly authorized, validly issued, fully paid and nonassessable. To the extent that additional shares of common stock may be issued in the future, the relative interests of the then existing stockholders may be diluted.

The shares of common stock outstanding before this offering are restricted securities as that term is defined in Rule 144 under the Securities Act. Restricted securities generally cannot be resold without registration or an exemption from registration.

#### WARRANTS

Each warrant entitles the holder to purchase one share of common stock at an exercise price of \$7.50 for a period of 24 months from the date of this prospectus, subject to our redemption rights described below. The warrants will be issued under the terms of a warrant agreement between Pacific Softworks and American Securities Transfer & Trust, Incorporated as warrant agent. Pacific Softworks has authorized and reserved for issuance the shares of common stock issuable on exercise of the warrants. The warrants are exercisable to purchase a total of 800,000 shares of common stock of Pacific Softworks. If the underwriter's over-allotment option relating to the warrants is exercised, the warrants are exercisable to purchase a total of 920,000 shares of common stock.

The warrant exercise price and the number of shares of common stock that may be purchased upon exercise of the warrants are subject to adjustment should any of the following events occur:

- a stock dividend on the common stock,
- a subdivision of the common stock,
- a recapitalization of the common stock,
- a reorganization of the common stock, or
- a merger or consolidation of Pacific Softworks with or into another corporation or business entity.

Commencing 30 days from the date of this prospectus and until the expiration of the warrants, Pacific Softworks may redeem outstanding warrants, in whole but not in part, upon not less than 30 days' notice, at a price of \$0.05 per warrant. This right to redeem outstanding warrants is conditioned upon the closing bid price of the common stock equaling or exceeding \$8.00 per share for 15 consecutive trading days. We must provide the redemption notice not more than five business days after conclusion of the 15 consecutive trading days in which the closing bid price of the common stock equals or exceeds \$8.00 per share.

In the event we exercise our right to redeem the warrants, the warrants will be exercisable until the close of business on the date fixed for redemption in our notice. If any warrant called for redemption is not timely exercised, that warrant will no longer be exercisable and the holder of that warrant will be entitled to the redemption price.

Pacific Softworks must have on file a current registration statement with the SEC pertaining to the common stock underlying the warrants for a holder to exercise the warrants or for the warrants to be redeemed by Pacific Softworks. The shares of common stock underlying the warrants must also be registered or qualified for sale under the securities laws of the states in

which the warrant holders reside. We intend to use our best efforts to keep the registration statement incorporating this prospectus current, but we can give no assurance that the registration statement (or any other registration statement we filed covering shares of common stock underlying the warrants) can be kept current. If the registration statement covering the underlying common stock is not kept current, or if the common stock underlying the warrants is not registered or qualified for sale in the state in which a warrant holder resides, the warrants may be deprived of any value.

Pacific Softworks is not required to issue any fractional shares of common stock upon the exercise of warrants or upon the occurrence of adjustments under anti-dilution provisions. Pacific Softworks will pay to holders of fractional interests an amount equal to the cash value of their fractional interests based upon the then-current market price of a share of common stock.

Warrants may be exercised upon surrender of the certificate representing those warrants on or before their expiration date (or earlier redemption date) at the offices of the warrant agent with the form of "Election to Purchase" on the reverse side of the warrant certificate completed and executed as indicated, accompanied by payment of the full exercise price by check payable to the order of Pacific Softworks for the number of warrants being exercised. Shares of common stock issued upon exercise of warrants for which payment has been received in accordance with the terms of the warrants will be fully paid and nonassessable.

The warrants do not confer upon the warrant holder any voting or other rights of a stockholder of Pacific Softworks. Upon notice to the warrant holders, Pacific Softworks has the right to reduce the exercise price or extend the expiration date of the warrants. Although this right is intended to benefit warrant holders, to the extent Pacific Softworks exercises this right when the warrants would otherwise be exercisable at a price higher than the prevailing market price of the common stock, the likelihood of exercise, and the resultant increase in the number of shares outstanding, may impede or make more costly a change in control of Pacific Softworks.

#### ANTI-TAKEOVER PROVISIONS

Our articles of incorporation and bylaws contain provisions that may make it more difficult for a third party to acquire, or may discourage acquisition bids for, Pacific Softworks. The board of directors of Pacific Softworks is authorized, without action of its stockholders, to issue authorized but unissued common stock and preferred stock. The existence of undesignated preferred stock and authorized but unissued common stock enables Pacific Softworks to discourage or to make it more difficult to obtain control of Pacific Softworks by means of a merger, tender offer, proxy contest or otherwise.

#### TRANSFER AGENT, WARRANT AGENT AND REGISTRAR

Pacific Softworks has retained American Securities Transfer & Trust, Incorporated to serve as the transfer agent and registrar for the common stock and warrant agent for the warrants.

#### SHARES ELIGIBLE FOR FUTURE SALE

On completion of this offering, Pacific Softworks will have 4,100,000 shares of common stock outstanding, assuming no warrants are exercised. If the underwriter's over-allotment option is exercised in full, 4,220,000 shares of common stock will be outstanding. Of these shares, 800,000 shares of common stock sold in this offering and any shares sold by Pacific Softworks upon exercise of the underwriter's over-allotment option will be freely transferable by persons

other than "affiliates" of Pacific Softworks as that term is defined under the Securities Act, without restriction or further registration. In addition, 200,000 shares beneficially owned by two persons who are not employees of Pacific Softworks and up to 160,000 shares issuable upon exercise of warrants to purchase units, are being registered concurrently with this offering. These securities may not be sold without the prior written consent of the underwriter for a period of 13 months from the date of this prospectus. These restrictions may be waived by the underwriter, although it has no current intention to do so.

The remaining 3,100,000 outstanding shares of common stock are "restricted securities" within the meaning of Rule 144 under the Securities Act and may not be sold in the absence of registration unless an exemption from registration is available, including the exemption contained in Rule 144. All of these shares become eligible for sale under Rule 144 commencing 90 days after the date of this prospectus. Under the terms of the underwriting agreement, the underwriter has required that the shares of common stock owned by officers, directors and the current stockholders may not be sold until at least 13 months from the date of this prospectus without the underwriter's prior written consent.

In general, under Rule 144, a stockholder who has beneficially owned shares of common stock for at least one year is entitled to sell, within any three-month period, a number of "restricted" shares that does not exceed the greater of 1% of the then outstanding shares of common stock or the average weekly trading volume during the four calendar weeks preceding such sale. Sales under Rule 144 are also subject to sale limitations, notice requirements and the availability of current public information about Pacific Softworks. Rule 144(k) provides that a stockholder who is not deemed to be an "affiliate" and who has beneficially owned shares of common stock for at least two years is entitled to sell those shares at any time under Rule 144(k) without regard to the limitations described above. In addition to the shares of common stock that are currently outstanding, a total of 320,000 shares of common stock have been reserved for issuance upon exercise of options granted under the equity incentive program.

Pacific Softworks is unable to estimate the number of shares that may be sold in the future by the existing holders of shares of our common stock or holders of options or warrants that are outstanding or the effect, if any, that sales of shares of common stock by these persons will have on the market price of the common stock prevailing from time to time. Sales of substantial amounts of common stock by these persons could adversely affect the then prevailing market prices of the common stock and warrants.

Pacific Softworks, its directors, executive officers and other stockholders have agreed with the underwriter that they will not sell any common stock without the prior consent of the underwriter for a period of 13 months from the date of this prospectus, except that Pacific Softworks may, without this consent, grant options and issue shares under its equity incentive program. The underwriter has no current intention to waive or shorten the lock-up arrangements.

Pacific Softworks intends to file a registration statement on Form S-8 under the Securities Act to register shares of common stock issued or reserved for issuance under outstanding options and our equity incentive program within 180 days after the date of this prospectus, thus permitting the resale of these shares by nonaffiliates in the public market without restriction under the Securities Act. Pacific Softworks intends to register these shares on Form S-8, along with common stock underlying options that have not been issued under our equity incentive program as of the date of this prospectus.

ADDITIONAL WARRANTS TO PURCHASE UNITS

Pacific Softworks also has issued warrants to purchase 40,000 units to members of Resch Polster Alpert & Berger LLP, special counsel to Pacific Softworks in this offering, and warrants to purchase an additional 40,000 units to two persons who have provided temporary accounting and administrative services to Pacific Softworks. Each of these warrants to purchase units may be exercised at any time over a period of 60 months commencing from the date of this prospectus at a price of \$5.25 per unit. These units are identical to the units sold in this offering. Pacific Softworks is also registering these units concurrently with this offering. The underwriter has required all holders of these units to not sell, transfer or convey any shares of common stock or warrants issued upon exercise of these warrants for 13 months after the date of this prospectus except upon consent of the underwriter.

#### OPTIONS TO GOLENBERG & CO.

In June 1998, Pacific Softworks agreed to issue options to Golenberg & Co., merchant bankers, if Golenberg & Co. introduces Pacific Softworks to a merger, acquisition or other transaction which is acceptable to Pacific Softworks before June 1999. To date, Golenberg & Co. has not introduced Pacific Softworks to any acceptable merger, acquisition or other transaction. These options would allow Golenberg & Co. the right to purchase up to 10% of the then outstanding capital stock of Pacific Softworks. If issued the options will be exercisable for a period of five years commencing from June 1998 for a total exercise price of \$400,000. In April 1999 Golenberg & Co. notified us that it was entitled to the options and that Golenberg & Co. would seek arbitration of the dispute under the rules of the American Arbitration Association. We believe there is no merit to the claims of Golenberg & Co. for these options.

#### UNDERWRITING

Subject to the terms and conditions of the underwriting agreement, Spencer Edwards, Inc. has agreed to purchase 800,000 units from Pacific Softworks. The underwriter will purchase the units at the price to public less underwriting discounts set forth on the cover page of this prospectus.

The underwriting agreement provides that the underwriter is committed to purchase all units offered in this offering, other than those covered by the over-allotment option described below, if the underwriter purchases any of these securities.

The underwriter has advised Pacific Softworks that the underwriter proposes to offer the units directly to the public at the price to public set forth on the cover page of this prospectus, and that it may allow to certain dealers that are members of the National Association of Securities Dealers, Inc., concessions not in excess of \$\_\_\_\_\_. The price to public, concessions and reallowance will not be charged until after the initial public offering is completed. After the initial public distribution of the units is completed, the shares of common stock and warrants will trade separately and their offering prices may change as a result of market conditions. No change in these terms will alter the amount of proceeds to be received by Pacific Softworks as set forth on the cover page of this prospectus. The underwriter has also advised Pacific Softworks that the underwriter does not intend to confirm sales to any accounts over which it exercises discretionary authority.

Pacific Softworks has agreed to pay the underwriter a nonaccountable expense allowance of 3% of the aggregate public offering price of the units offered, including units sold on exercise of the over-allotment option. Pacific Softworks paid the underwriter \$35,000 before the date of this prospectus as an advance against this nonaccountable expense allowance. Pacific Softworks

has also agreed to pay all expenses in connection with qualifying the units for sale under the laws of various states designated by the underwriter.

Pacific Softworks has granted the underwriter an option, exercisable for 45 days after the date of this prospectus, to purchase up to 120,000 additional units at the same price as the initial units offered. The underwriter may purchase the units solely to cover over-allotments, if any, in connection with the sale of the units offered in the offering. If the underwriter fully exercises its over-allotment option, the total public offering price, underwriting discounts and proceeds to Pacific Softworks will be \$4,830,000, \$483,000 and \$4,347,000, respectively.

The underwriter may engage in over-allotment, stabilizing transactions and covering transactions. Over-allotment involves sales in excess of the offering size, which create a short position. Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum. Covering transactions involve purchases of the securities in the open market after the distribution has been completed in order to cover short positions. These stabilizing transactions and covering transactions may cause the price of the common stock or warrants to be higher than they would otherwise be in the absence of these transactions.

Neither Pacific Softworks nor the underwriter makes any representation or prediction as to the direction or magnitude of any effect that the transactions described above may have on the price of the common stock or warrants. In addition, neither Pacific Softworks nor the underwriter makes any representation that the underwriter will engage in these transactions or that these transactions, once commenced, will not be discontinued without notice.

Our officers, directors and stockholders have agreed not to offer, sell or otherwise dispose of any shares of common stock or derivative securities of Pacific Softworks for a period of 13 months after the date of this prospectus without the prior written consent of the underwriter. The underwriter has agreed that Pacific Softworks may file an S-8 registration statement 180 days after the date of this prospectus registering common stock underlying outstanding options and options to be granted under the equity incentive program. However, sales of common stock so registered:

- may not exceed an aggregate of 25,000 shares until expiration of the 13 month lockup arrangement, and
- may only be made by persons not serving as officers or directors of Pacific Softworks.

The underwriter has no present intention to waive or shorten the period of the lock-up arrangements.

Pacific Softworks will sell to the underwriter on completion of the offering, for a total purchase price of \$100, the underwriter's option for the purchase of units entitling the underwriter or its assigns to purchase one unit for each 10 units sold to the public (excluding the units sold in the over-allotment option). The underwriter's option will be exercisable on the date of this prospectus and will expire five years from that date. For each warrant included in the units underlying the underwriter's option, the underwriter will be able to purchase one share of common stock at an exercise price of \$7.50 per share during the exercise period of these warrants. The rights and attributes of these warrants issuable to the underwriter are identical to the warrants



included in the units sold in the offering. The exercise price of the underwriter's option to purchase units is 120% of the public offering price or \$6.30 per unit.

Pacific Softworks will set aside and at all times have available a sufficient number of securities to be issued upon exercise of the underwriter's option. The underwriter's option and underlying securities will be restricted from sale, transfer, assignment or hypothecation for a period of one year after the date of this prospectus, except to officers of the underwriter, selling group members, and their officers, employees or partners. Thereafter, the underwriter's option and underlying units will be transferable provided that transfers are made in accordance with the provisions of the Securities Act. Pacific Softworks has agreed, at the request of the underwriter, to register the common stock included in the units and underlying the warrants included in the units issuable upon exercise of the underwriter's option.

For a period of three years from the date of this prospectus, the underwriter has a preferential right to purchase for its account or to sell for the account of Pacific Softworks (or any successors), or any subsidiaries of Pacific Softworks, any securities with respect to which any of them may seek to sell, publicly or privately, for cash other than transactions with a lending institution.

Pacific Softworks and the underwriter have entered into a non-exclusive agreement which provides that, if the underwriter arranges for the purchase or sale of substantially all of the assets of Pacific Softworks, or for a merger, consolidation or acquisition accepted by Pacific Softworks during the five-year period commencing on the date of this prospectus, the underwriter will receive a fee based on a sliding scale ranging from 5% of the first \$1 million of consideration and decreasing to 3% of consideration in excess of \$2 million.

Pacific Softworks and the underwriter have entered into an agreement which provides that for a period of three years from the date of this prospectus, all public sales of our securities by officers, directors and principal stockholders of Pacific Softworks at the time of this prospectus shall be effected through or with the underwriter on an exclusive basis, provided that the underwriter offers the best price reasonably available. In addition, for a period of three years starting two years from the date of this prospectus, in the case of private transactions in our common stock, these selling security holders must offer the underwriter the exclusive opportunity to purchase or sell the common stock on terms at least as favorable as the selling security holder can obtain elsewhere.

For a period of five years after the date of this prospectus, the underwriter has the right to have an observer attend meetings of our board of directors. This observer will be reimbursed for expenses incurred in attending any meeting.

Before this offering, there was no public market for our securities. The public offering price of the units and the exercise price of the warrants were determined by arms-length negotiation between Pacific Softworks and the underwriter. There is no direct relation between the offering price of the units and the assets, book value or net worth of Pacific Softworks. Among the factors considered by Pacific Softworks and the underwriter in pricing the units and in determining the exercise price of the warrants were the results of operations, the current financial condition and future prospects of Pacific Softworks, the experience of management, the amount of ownership to be retained by present stockholders, the general condition of the economy and the securities markets and the demand for securities of companies considered comparable to Pacific Softworks.

In connection with this offering, Pacific Softworks and the underwriter have agreed to indemnify each other against certain liabilities, including liabilities under the Securities Act, and if indemnification is unavailable or insufficient, Pacific Softworks and the underwriter have agreed to damage contribution arrangements based upon relative benefits received from this offering and relative fault resulting in such damage.

#### LEGAL MATTERS

The validity of the securities offered hereby will be passed on for Pacific Softworks by Resch Polster Alpert & Berger LLP, Los Angeles, California. Members of Resch Polster Alpert & Berger LLP own warrants to acquire a total of 40,000 units. Certain legal matters in connection with the offering will be passed on for the underwriter by Berliner Zisser Walter & Gallegos, P.C., Denver, Colorado.

#### EXPERTS

Merdinger, Fruchter, Rosen & Corso, P.C., independent auditors, have audited the consolidated financial statements of Pacific Softworks for the years ended December 31, 1996, 1997 and 1998, as set forth in their report, which is included in this prospectus. Pacific Softworks consolidated financial statements are included in this prospectus in reliance on their report, given on their authority as experts in accounting and auditing.

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
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TO THE BOARD OF DIRECTORS  
PACIFIC SOFTWARES, INC. AND SUBSIDIARY

We have audited the accompanying consolidated balance sheets of PACIFIC SOFTWARES, INC. AND SUBSIDIARY as of December 31, 1998 and 1997, and the related consolidated statements of operations, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1998. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 consolidated financial position of PACIFIC SOFTWARES, INC. AND SUBSIDIARY as of December 31, 1998 and 1997, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1998 in conformity with generally accepted accounting principles.

MERDINGER, FRUCHTER, ROSEN & CORSO, P.C.  
Certified Public Accountants

Los Angeles, California  
January 29, 1999, except  
for Note 14 as to which the  
date is March 15, 1999

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
CONSOLIDATED BALANCE SHEETS

	December 31, 1997	31, 1998	March 31, 1999 (Unaudited)
<b>ASSETS</b>			
<b>Current assets</b>			
Cash	\$ 624,952	\$ 224,031	\$ 460,907
Accounts receivable, net of allowance for doubtful accounts of \$36,400, \$86,400 and \$86,400	337,690	268,902	442,091
Related party receivable	--	43,000	--
Other receivable	2,125	--	25,000
Prepaid expenses	36,112	15,523	15,523
Total current assets	1,000,879	551,456	943,521
<b>Fixed assets, net of accumulated depreciation and amortization of \$311,204, \$348,761 and \$362,221</b>			
	69,158	82,196	95,464
<b>Other assets</b>			
Trademark	1,034	1,188	1,188
Security deposit	--	8,486	9,025
Deferred offering costs	--	--	281,541
Total assets	\$ 1,071,071	\$ 643,326	\$ 1,330,739
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
<b>Current liabilities</b>			
Accounts payable and accrued expenses	\$ 219,027	\$ 180,469	\$ 388,069
Related party payable	--	103,705	--
Accrued taxes payable	20,601	21,705	9,357
Customer deposits	--	23,100	--
Total current liabilities	239,628	328,979	397,426
Deferred revenue	140,811	106,874	113,874
Commitments and contingencies	--	--	--
Minority interest			
<b>Stockholders' equity</b>			
Preferred stock, \$.01 par value; 10,000,000 shares authorized, no shares issued and outstanding	--	--	--
Common stock, \$.001 par value; 50,000,000 shares authorized, 3,200,000, 3,200,000 and 3,300,000 shares issued and outstanding	3,200	3,200	3,300
Additional paid-in capital	174,658	174,658	874,558
Retained earnings (deficit)	492,212	18,452	(41,013)
Cumulative adjustment for currency translation	20,562	11,163	(17,406)
Total stockholders' equity	690,632	207,473	819,439
Total liabilities and stockholders' equity	\$ 1,071,071	\$ 643,326	\$ 1,330,739

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

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,			Three Months Ended March 31,	
	1996	1997	1998	1998	1999
	-----	-----	-----	-----	-----
	(Unaudited)				
Net revenue:					
Sales	\$ 3,123,893	\$ 2,929,536	\$ 2,479,589	\$ 679,092	\$ 713,059
Royalties and other	564,217	380,248	307,808	16,987	58,591
Total	----- 3,688,110	----- 3,309,784	----- 2,787,397	----- 696,079	----- 771,650
Cost of revenue -					
Purchases and royalty fees	96,576	116,311	100,336	27,843	30,336
Gross profit	----- 3,591,534	----- 3,193,473	----- 2,687,061	----- 668,236	----- 741,314
Expenses:					
Selling, general and administrative	2,257,560	2,110,038	1,936,117	386,447	380,815
Research and development	632,811	834,049	851,568	213,703	323,824
Depreciation and amortization	72,415	64,195	58,850	14,713	13,460
Former officer's consulting and administrative expense	235,714	314,286	314,286	82,680	82,680
Total expenses	----- 3,198,500	----- 3,322,568	----- 3,160,821	----- 697,543	----- 800,779
Income (loss) before income taxes	393,034	(129,095)	(473,760)	(29,307)	(59,465)
Income tax expense	--	--	--	--	--
Net income (loss)	----- \$ 393,034	----- \$ (129,095)	----- \$ (473,760)	----- \$ (29,307)	----- \$ (59,465)
Net income (loss) per share - Basic and diluted	=====	=====	=====	=====	=====
	\$ 0.12	\$ (0.04)	\$ (0.14)	\$ (0.01)	\$ (0.02)
Weighted average number of shares outstanding	=====	=====	=====	=====	=====
	3,340,000	3,340,000	3,340,000	3,340,000	3,378,888

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

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	For the Years Ended December 31, 1996	1997	1998	Three Months Ended March 31, 1998	1999
	-----	-----	-----	-----	-----
	(Unaudited)				
Net income (loss)	\$ 393,034	\$(129,095)	\$(473,760)	\$ (29,307)	\$ (59,465)
Other comprehensive income (loss)					
Foreign currency translation adjustment	19,219	49,946	(9,399)	(39,979)	(28,569)
	-----	-----	-----	-----	-----
Comprehensive income (loss)	\$ 412,253	\$ (79,149)	\$(483,159)	\$ (69,286)	\$ (88,034)
	=====	=====	=====	=====	=====

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

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Common Stock		Additional Paid - in Capital	Retained Earnings	Cumulative Foreign Currency Translation Adjustment	Total Stockholders' Equity
	Shares	Amount				
Balance, January 1, 1996	3,200,000	\$ 3,200	\$ 174,658	\$ 228,273	\$ (48,603)	\$ 357,528
Foreign currency translation adjustment	--	--	--	--	19,219	19,219
Net income	--	--	--	393,034	--	393,034
Balance, December 31, 1996	3,200,000	3,200	174,658	621,307	(29,384)	769,781
Foreign currency translation adjustment	--	--	--	--	49,946	49,946
Net loss	--	--	--	(129,095)	--	(129,095)
Balance, December 31, 1997	3,200,000	3,200	174,658	492,212	20,562	690,632
Foreign currency translation adjustment	--	--	--	--	(9,399)	(9,399)
Net loss	--	--	--	(473,760)	--	(473,760)
Balance, December 31, 1998	3,200,000	3,200	174,658	18,452	11,163	207,473
Private placement of common stock	100,000	100	499,900			500,000
Warrants issued in connection with offering	--	--	200,000	--	--	200,000
Foreign currency translation adjustment	--	--	--	--	(28,569)	(28,569)
Net loss	--	--	--	(59,465)	--	(59,465)
Balance, March 31, 1999	3,300,000	\$ 3,300	\$ 874,558	\$ (41,013)	\$ (17,406)	\$ 819,439

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



PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Years Ended	December 31,	Three Months Ended		
	1996	1997	1998	March 31,	
	-----	-----	-----	-----	
				1998	
				1999	
				-----	
				(Unaudited)	
				-----	
Cash flows from operating activities:					
Net income (loss)	\$ 393,034	\$(129,095)	\$(473,760)	\$ (29,307)	\$ (59,465)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:					
Depreciation and amortization	72,415	64,195	58,850	14,713	13,460
Bad debts	--	--	50,000	--	--
(Increase) decrease in assets:					
Accounts receivable	(247,081)	305,048	18,788	(148,758)	(173,189)
Related party receivable	--	--	(43,000)	--	43,000
Other receivables	(23,216)	22,152	2,125	2,125	(25,000)
Prepaid expenses	(16,600)	10,990	20,589	5,512	--
Deposits and trademark	458	392	(8,486)	(91)	(539)
Increase (decrease) in liabilities:					
Accounts payable and accrued expenses	87,710	(44,532)	(38,558)	32,014	(207,600)
Related party payable	--	--	3,705	--	(3,705)
Accrued taxes payable	1,867	13,771	1,104	(12,796)	(12,348)
Customer deposits	--	--	23,100	--	(23,100)
Deferred revenue	63,898	43,646	(33,937)	--	7,000
Net cash provided by (used in) operating activities	332,485	286,567	(419,480)	(136,588)	(26,286)
Cash flows used for investing activities:					
Acquisition of fixed assets	(14,493)	(19,903)	(71,888)	(6,421)	(27,982)
Cash flows from financing activities:					
Private placement of common stock	--	--	--	--	500,000
Acquisition of stock in subsidiary	(5,743)	(5,555)	(5,500)	(5,500)	--
Proceeds of borrowings	--	--	150,000	--	--
Repayment of borrowings	(200,000)	--	(50,000)	--	(100,000)
Deferred offering costs	--	--	--	--	(81,541)
Net cash (used) provided by financing activities	(205,743)	(5,555)	94,500	(5,500)	318,459
Effect of exchange rate changes on cash	25,114	55,501	(4,053)	(13,917)	(27,315)
Net increase (decrease) in cash	137,363	316,610	(400,921)	(162,426)	236,876
Cash - Beginning	170,979	308,342	624,952	624,952	224,031
Cash - Ending	\$ 308,342	\$ 624,952	\$ 224,031	\$ 462,526	\$ 460,907
	=====	=====	=====	=====	=====
Supplemental cash flow information:					
Cash paid during the year for -					
Interest	\$ 42	\$ --	\$ 482	\$ --	\$ --
	=====	=====	=====	=====	=====
Supplemental non-cash financing activities:					
During the period ended March 31, 1999, warrants valued at \$200,000 were issued in connection with the public offering.					

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

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 1998

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Pacific Softworks, Inc., incorporated in California in November 1992, develops and licenses Internet and Web related software and software development tools. Its products enable Internet and Web based communications, based on a set of rules known as protocols, and are embedded into systems and "information appliances" developed or manufactured by others. Information appliances are Internet connected versions of everyday products such as telephones, televisions, fax machines and other digitally based devices. Its operations are conducted principally from its offices in Southern California, and it maintains sales offices in England and Japan.

Basis of Consolidation

The consolidated financial statements include the accounts of Pacific Softworks, Inc. ("PSI") and its wholly owned subsidiary, Network Research Corp. Japan, Ltd. ("NRC"). Accordingly, all references herein to PSI or the "Company" include the consolidated results of its subsidiary. All significant intercompany accounts and transactions have been eliminated in consolidation.

In January of 1998, PSI purchased the remaining 21% of NRC stock held by a third party, to increase its holdings to 100%. The purchase price was \$5,000. The acquisition has been accounted for as a purchase.

All of NRC's operations and assets are located in the country of Japan.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with original maturities of three months or less to be cash equivalents.

Revenue Recognition

The Company is engaged primarily as a developer and licensor of software and generates revenue primarily from the one-time sales of licensed software. Generally, revenue is recognized upon shipment of the licensed software. For multiple element license arrangements, the license fee is allocated to the various elements based on fair value. When a multiple element arrangement includes rights to a post-contract customer support, the portion of the license fee allocated to each function is recognized ratably over the term of the arrangement.

Use of Estimates

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

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 1998

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Depreciation and Amortization

Furniture, fixtures and equipment are stated at cost and depreciated using both the straight-line and double declining balance methods over their estimated useful lives, generally five to seven years. Purchased computer software costs have been amortized over five years.

The costs of maintenance and repairs are charged to expense when incurred; costs of renewals and betterments are capitalized. Upon the sales or retirement of property and equipment, the cost and related accumulated depreciation are eliminated from the respective accounts and the resulting gain or loss is included in operations.

Fair Value of Financial Instruments

The Company's financial instruments consist of cash, accounts receivable, accounts payable and short-term debt. The carrying amounts of cash, accounts receivable, accounts payable and short-term debt approximate fair value due to highly liquid nature of these short-term instruments.

Long-Lived Assets

Long-lived assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may not be recoverable. When required, impairment losses on assets to be held and used are recognized based on the fair value of the assets and long-lived assets to be disposed of are reported at the lower of carrying amount of fair value less cost to sell.

Income Taxes

The Company has been a subchapter S corporation. Income is passed through to the stockholders who pay personally their share of the applicable taxes. Therefore, no provision for income taxes is made at December 31, 1996, 1997 and 1998. (See Note 14).

Subsequent to the termination of the Company's S Corporation election, provisions for income taxes are based on taxes payable or refundable for the current year and deferred taxes on temporary differences between the amount of taxable income and pretax financial income and between the tax bases of assets and liabilities and their reported amounts in the financial statements. Deferred tax assets and liabilities are included in the financial statements at currently enacted income tax rates applicable to the period in which the deferred tax assets and liabilities are expected to be realized or settled as prescribed SFAS No. 109, "Accounting for Income Taxes." As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Translation of Foreign Currency

The Company translates the foreign currency financial statements of its foreign subsidiary in accordance with the requirements of Statement of Financial Accounting Standards No. 52, "Foreign Currency Translation". Assets and liabilities are translated at current exchange rates and related revenues and expenses are translated at average exchange rates in effect during the period. Resulting translation adjustments are recorded as a separate component in stockholders' equity. Foreign currency transaction gains and losses are included in determining net income.

Concentration of Credit Risk

The Company places its cash in what it believes to be credit-worthy financial institutions. However, cash balances may exceed FDIC insured levels at various times during the year.



PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS

## NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

## Advertising Costs

Advertising costs, except for costs associated with direct-response advertising, are charged to operations when incurred. The costs of direct-response advertising, if any, are capitalized and amortized over the period during which future benefits are expected to be received.

## Per Share of Common Stock

In February 1997, the Financial Accounting Standards Board issued a new statement titled "Earnings Per Share" (SFAS No. 128). This statement is effective for both interim and annual periods ending after December 15, 1997 and specifies the computation, presentation, and disclosure requirements for earnings per share for entities with publicly held common stock or potential common stock. All prior-period earnings per share data presented has been restated to conform with the provisions for SFAS No. 128.

Per share amounts have been computed based on the average number of shares of common stock outstanding during each period. In connection with the Company's proposed initial public offering ("IPO"), stock options issued for consideration below the IPO per share price during the twelve months before the filing of the registration statement are considered to be similar to a stock dividend or stock split and have been included in the calculation of shares of common stock outstanding for all periods presented.

## Stock Based Compensation

The Company uses the intrinsic value method of accounting for stock-based compensation in accordance with Accounting Principles Board Opinion No. 25. See Note 10 for proforma disclosure of net income and earnings per share under the fair value method of accounting for stock-based compensation as proscribed by Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123.

## Comprehensive Income

In June 1997, the Financial Accounting Standards Board issued a new statement titled "Reporting Comprehensive Income" (SFAS No. 130). This statement is effective for both interim and annual periods beginning after December 15, 1997. This statement uses the term "comprehensive income" to describe the total of all components of comprehensive income, including net income. This statement uses the term "other comprehensive net income" to refer to revenues, expenses, gains or losses that under generally accepted accounting principles are included in comprehensive income, but excluded from net income.

## Interim Financial Information

The unaudited financial information furnished herein reflects all adjustments, consisting only of normal recurring adjustments, which, in the opinion of management, are necessary to fairly state the Company's financial position, the results of its operations and cash flows for the periods presented. The results of operations for the three months ended March 31, 1999 are not necessarily indicative of results for the entire fiscal year ending December 31, 1999.

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS

## NOTE 2 - FIXED ASSETS

Fixed assets consist of the following:

	December 31,			March 31,	
	1996	1997	1998	1998	1999
Furniture, fixtures and equipment	\$124,764	\$144,533	\$216,421	150,954	243,149
Computer software	235,829	235,829	214,536	235,829	214,536
	360,593	380,362	430,957	386,783	457,685
Less: accumulated depreciation and amortization	247,143	311,204	348,761	325,917	362,221
Fixed assets - net	\$113,450	\$ 69,158	\$ 82,196	60,866	95,464
Depreciation expense recorded in the statement of operations	\$ 25,647	\$ 19,348	\$ 30,243	\$ 7,563	\$ 13,460
Unamortized computer software costs	\$ 71,514	\$ 28,607	\$ --	\$ 21,457	\$ --
Amortization of computer software costs	\$ 46,768	\$ 42,907	\$ 28,607	\$ 7,150	\$ --

## NOTE 3 - DEFERRED REVENUE

The Company provides technical support for its products, usually over a twelve-month term. Revenue is recognized as earned on a straight-line basis

## NOTE 4 - RELATED PARTY TRANSACTIONS

a) As of December 31, 1998, the Company has advanced funds to its principal stockholder in the amount of \$43,000. The advances bear no interest and are repayable upon demand. (See Note 14).

b) As of December 31, 1998, the Company has received advances from a company controlled by the spouse of the principal stockholder of PSI. The advances totaled \$103,705. The advances bear no interest and are repayable upon demand. (See Note 14).

c) The company mentioned in item (b) above also occupies space in premises leased by PSI. The Company believes that the terms of occupancy are no less favorable than those that could be obtained from unaffiliated third parties. This party is expected to relocate during the first half of 1999.

d) The principal stockholder of the Company has personally guaranteed any advances made to the Company pursuant to a line of credit provided by Bank of America. Total availability under the line is \$250,000. No advances were outstanding as of December 31, 1998.

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 1998

NOTE 5 - CAPITAL STOCK

- a) The Company is authorized to issue 10,000,000 shares of Preferred Stock, par value \$.01. Preferred shares may be issued from time to time in one or more series. The number of shares in each series and the designation of each series to be issued shall be determined from time to time by the board of directors of the Company.
- b) On January 30, 1998, the Company increased the number of shares of common stock it is authorized to issue from 1,000,000 shares to 50,000,000 shares. In June of 1998, the Company effected a stock split and subsequently effected a reverse stock split. The net result of these two stock transactions was an effective 6.27205 shares for one stock split, increasing the outstanding shares from 510,200 to 3,200,000.

All references in the accompanying financial statements to the number of shares of common stock and per-share amounts for 1996, 1997, 1998 and 1999 have been restated to reflect the effective stock split.

NOTE 6 - STOCK PLAN

On April 17, 1998, the Company adopted the 1998 Equity Incentive Program (the "Plan"). The Plan provides for the granting of the following Stock Awards: (i) Incentive Stock Options, (ii) Non-Statutory Stock Options, (iii) Stock Appreciation Rights, (iv) Stock Bonuses, and (v) Rights to acquire Restricted Stock. Persons eligible to receive Stock Awards are the employees, directors and consultants of the Company and its Affiliates, as defined. Incentive Stock Options may be granted only to employees. Stock awards other than Incentive Stock Options may be granted to all eligible persons.

The maximum term of any options granted is ten years. Vesting requirements may vary, and will be determined by the board of directors.

The number of shares reserved for issuance under the Plan is 320,000 shares. (See Note 10).

NOTE 7 - ADVERTISING COSTS

Advertising costs incurred and recorded as expense in the statement of operations were \$222,051, \$263,912 and \$213,670 for the years ended December 31, 1996, 1997 and 1998, respectively, and were \$59,259 and \$43,999 for the three months ended March 31, 1998 and 1999, respectively.

NOTE 8 - INTEREST COSTS

Interest costs incurred were \$42, (\$43) and \$6,004 in 1996, 1997 and 1998, respectively, all of which were charged to operations.

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
 NOTES TO FINANCIAL STATEMENTS  
 DECEMBER 31, 1998

NOTE 9 - INCOME TAXES AND S CORPORATION STOCKHOLDER DISTRIBUTIONS

a) S Corporation Election

Effective January 1, 1995, the Company, with the consent of its stockholders, elected under the Internal Revenue Code to be an S corporation. For 1996, 1997 and 1998, the stockholders of the Company were taxed on their proportional share of the corporation's taxable income, or deducted personally any corporate losses. Therefore, no provision or liability or carry-forward loss for federal income taxes has been included in these financial statements.

b) Distributions

The Company has paid no distributions to its stockholders.

c) Tax Provision

As a result of the Company's tax status as an S Corporation, operating results as presented in the accompanying consolidated financial statements do not include a provision for income taxes for the years ended December 31, 1996, 1997 and 1998.

d) Proforma Income Taxes

Proforma income taxes (benefit), assuming that the Company had not been an S Corporation in each of the periods presented, are as follows:

	1996 -----	1997 -----	1998 -----
Federal	\$ 90,410	\$ 3,100	\$ (93,510)
State	28,174	2,500	(30,674)
	-----	-----	-----
	\$ 118,584	\$ 5,600	\$(124,184)
	=====	=====	=====

NOTE 10 - STOCK OPTIONS

a) The Company has granted certain non-statutory options to purchase shares of Common Stock to two employees. Each option is for 70,000 shares at an exercise price of \$1.25 per share. The options vest on January 1, 1999 and expire June 25, 2008.

b) In 1999, the company granted certain non-statutory option to purchase shares of Common Stock to three directors. Each option is for 15,000 shares at an exercise price of \$5.00 per share. The options vest immediately and expire in 2008.

c) Plan and non-plan stock option activity is summarized as follows:

	December 31,			March 31,
	1996	1997	1998	1999
	-----	-----	-----	-----
Outstanding at beginning of period	--	--	--	140,000
Options granted at an exercise price of \$5.00 per share	--	--	--	45,000
Options granted at an exercise price of \$1.25 per share	--	--	140,000	--
	-----	-----	-----	-----
Outstanding at end of period	--	--	140,000	185,000
	=====	=====	=====	=====
Exercisable at end of period	--	--	--	185,000



	=====	=====	=====	=====
Weighted average exercise price of options outstanding	\$ --	\$ --	\$ 1.25	\$ 2.16
	=====	=====	=====	=====
Weighted average remaining contractual life of options outstanding	--	--	9 1/2 years	9 1/2 years

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 1998

NOTE 10 - STOCK OPTIONS (continued)

The Company accounts for its stock option transactions under the provisions of APB No. 25. The following proforma information is based on estimating the fair value of grants based upon the provisions of SFAS No. 123. The fair value of each option granted during the period ended December 31, 1998 has been estimated as of the date of grant using the Black-Scholes option pricing model with the following assumptions: risk free interest rate of 5.5%, life of options of 10 years, and expected dividend yield of 0%. The fair value of each option granted during the period ended March 31, 1999 has been estimated with the following assumptions: risk free interest rate of 5.5%, life of options of 10 years and expected dividend yield of 0%. Under these assumptions, the weighted average fair value of options granted during the periods ending December 31, 1998 and March 31, 1999 was \$0.52 and \$2.09, respectively. Accordingly, the Company's proforma net loss and net loss per share assuming compensation cost was determined under SFAS No. 123 would have been the following:

	Year Ended December 31, 1998 -----	Three Months Ended March 31, 1999 -----
Net Loss	\$ (546,560)	\$ (67,298)
Net Loss Per Share	\$ (0.16)	\$ (0.02)

NOTE 11 - SEGMENTED INFORMATION

The Company's assets are located principally in the United States. Product sales are to the following geographic areas:

	Years Ended December 31, -----			Three Months Ended March 31, -----	
	1996 ----	1997 ----	1998 ----	1998 ----	1999 ----
United States and the Americas	50%	50%	43%	59%	44%
Europe and the United Kingdom	17%	35%	40%	38%	42%
Asia and Australia	27%	15%	17%	3%	14%

NOTE 12 - EARNINGS PER SHARE

Stock options issued with an exercise price below the IPO purchase price during the twelve months before the filing of the registration statement have been included in the calculation of shares of common stock outstanding as if they had been outstanding for all periods presented. The amount of such shares included in earnings per share calculations totals 140,000.

NOTE 13 - COMMITMENTS AND CONTINGENCIES

- a) The Company occupies facilities under terms of an operating lease expiring September 15, 2000. Rent expense included in the statement of operations totaled \$30,000, \$56,100 and \$106,592 in 1996, 1997 and 1998, respectively and \$823 and \$27,676 for the three months ended March 31, 1998 and 1999, respectively. The Company leases an auto under term of an operating lease expiring August 31, 1999. Auto lease expense included in the statement of operations totaled \$0, \$5,171 and \$15,513 in 1996, 1997 and 1998, respectively and \$0 and \$3,878 for the three months ended March 31, 1998 and 1999, respectively.



PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
 NOTES TO FINANCIAL STATEMENTS  
 DECEMBER 31, 1998

NOTE 13 - COMMITMENTS AND CONTINGENCIES

Future minimum lease payments are as follows:

1999	\$114,894
2000	76,608

- b) The Company maintains a revolving line of credit arrangement with Bank of America. The credit limit under the arrangement is \$250,000. Advances, when drawn upon, bear interest at the Bank's Reference Rate plus two percent (9.75% at December 31, 1998). Advances are collateralized by the Company's accounts receivable and inventory and are secured by the personal guaranty of the Company's principal stockholder.

No advances were outstanding under the line at December 31, 1998.

- c) The Company is obligated to a former officer and 49% stockholder for a consulting agreement, covenant not to compete and buy-out of an employment agreement (collectively, the "Agreement"). The obligation provides for a monthly payment of \$26,190.49 over a 42 month period. At December 31, 1998, nine payments remain. In addition to these payments, the Agreement requires that so long as the Company has not paid in full all obligations under the Agreement, it is restricted from making any distributions to stockholders, other than necessary for any tax liability resulting from corporate earnings; is prohibited from issuing securities; is prohibited from paying executive compensation in excess of certain levels; and accelerates payment of obligations under the Agreement if certain corporate income levels are not met. The obligations under the Agreement are secured by substantially all of the outstanding shares of common stock of the Company and all assets of the Company.

The former officer and stockholder has given his consent to the sale of common stock described in Note 14(c).

- d) In June 1998, the Company agreed, subject to the conditions described below, to issue options to a consultant equal in number to 10% of the Company's then outstanding capital stock. These options will be issued if the consultant introduces the Company to a merger, acquisition or other transaction which is acceptable to the Company before June 1999. To date, the consultant has not introduced any such transaction to the Company. If issued, the options will be exercisable for a period of five years commencing from June 1998 at an exercise price of \$1.20 per share.

PACIFIC SOFTWARES, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 1998

NOTE 14 - SUBSEQUENT EVENTS

- a) Subsequent to December 31, 1998, the Company paid in full the liability to the related party described in Note 4(b).
- b) Subsequent to December 31, 1998, the related party receivable described in Note 4(a) was repaid.
- c) In February 1999 the Company sold 100,000 units to a single accredited investor at a price of \$5.00 per unit for total proceeds of \$500,000. Each unit consisted of one share of common stock and one common stock purchase warrant entitling the holder thereof to purchase one share of common stock for two years at an exercise price of \$6.00 per share.
- d) As a result of the sale of common stock described in item (c) above, the Company's S Corporation election has been terminated as of February 14, 1999.
- e) In February 1999, the Company entered into a letter of intent with an underwriter in connection with a proposed initial public offering of the Company's securities. The letter of intent relates to the proposed sale by the Company of 800,000 units. Each unit will consist of one share of common stock and one warrant. Each warrant will entitle the holder to purchase one share of common stock at an exercise price of \$7.50 for a period of two years commencing from the initial issuance. Under the letter of intent, the underwriters will also be granted the right to purchase up to an additional 120,000 units for the sole purpose of covering over-allotments. It is expected that the units will be offered to the public at an offering price of \$5.25 per unit.
- f) Warrants to purchase 80,000 units have been issued to certain professionals who have rendered legal, temporary accounting and administrative services to the Company. Each of these warrants to purchase units may be exercised at any time over a period of 60 months commencing from the date of the Company's prospectus at a price of \$5.25 per unit. These units are identical to the units to be sold by the Company in the proposed IPO. The warrants have been valued at \$200,000.
- g) Upon completion of the IPO, the Company will issue to the representative of the underwriters options to purchase one unit for each 10 units sold to the public. The options will be exercisable commencing one year from the effective date of the registration statement and for a period of four years thereafter. The exercise price of the option is \$6.30 per unit.

800,000 Units

Pacific Softworks, Inc.

[Company Logo]

Consisting of

800,000 shares of common stock

and

800,000 warrants.

Spencer Edwards, Inc.

May , 1999

-----  
PROSPECTUS  
-----

Until \_\_\_\_\_, 1999 (25 days after the date of this prospectus), all dealers effecting transactions in the units, common stock and warrants, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the obligations of dealers to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission or any applicable state securities commission becomes effective. This preliminary prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

PROSPECTUS

Subject to Completion, Dated May \_\_, 1999

[PACIFIC SOFTWARES, INC. LOGO]

80,000 UNITS  
CONSISTING OF 80,000 SHARES OF COMMON STOCK AND  
80,000 WARRANTS  
AND  
200,000 SHARES

The security holders named in this prospectus may sell for their accounts up to 80,000 units and 200,000 shares of common stock of Pacific Softworks. Each unit consists of one share of common stock and one warrant. The common stock and warrants will trade separately.

Each warrant allows its holder to purchase for a period of 24 months one share of common stock at a price of \$7.50. Pacific Softworks reserves the right to redeem all outstanding warrants at \$0.05 per warrant if the closing bid price of our common stock equals or exceeds \$8.00 per share for 15 consecutive trading days.

The securities described in this prospectus are not being sold by any underwriter. Pacific Softworks will not receive any proceeds from the sale of these securities.

Pacific Softworks expects to list the common stock and warrants on the Nasdaq SmallCap Market under the symbols "PASW" and "PASWw."

INVESTING IN THESE SECURITIES INVOLVES A HIGH DEGREE OF RISK. SEE "RISK FACTORS" BEGINNING ON PAGE 6

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED THESE SECURITIES OR PASSED UPON THE ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The date of this prospectus is May \_\_, 1999

## SALE OF SECURITIES DESCRIBED IN THIS PROSPECTUS.

The sale of the securities described in this prospectus may be made from time to time in transactions, which may include block transactions by or for the account of the holders, in the over-the-counter market or in negotiated transactions through a combination of these methods of sale or otherwise. Sales may be made at fixed prices which may be changed, at market prices prevailing at the time of sale, or at negotiated prices.

A post-effective amendment to the registration statement that includes this prospectus must be filed and declared effective by the Securities and Exchange Commission before a holder may:

- sell any securities described in this prospectus according to the terms of this prospectus either at a fixed price or a negotiated price, either of which is not the prevailing market price,
- sell securities described in this prospectus in a block transaction to a purchaser who resells,
- pays compensation to a broker-dealer that is other than the usual and customary discounts, concessions or commissions, or
- makes any arrangements, either individually or in the aggregate, that would constitute a distribution of the securities described in this prospectus.

Information contained in this prospectus, except for the cover page, the back cover page and the information under the heading "Selling Security Holders", is a part of that separate prospectus relating to a concurrent initial public offering by Pacific Softworks. This prospectus contains information, including all information relating to the concurrent underwritten offering and the underwriter, that may not be pertinent to the sale of the securities offered in this prospectus by the holders.

The securities described in this prospectus may be sold by the holders or their transferees starting on the date of this prospectus. The holders have agreed with Spencer Edwards, Inc. not to sell any of their securities for a period of 13 months from the date of this prospectus without the prior written consent of the underwriter. Sales of these securities may depress the price of the common stock and the warrants in any market that may develop for these securities.



## SELLING SECURITY HOLDERS

This prospectus relates to the sale of 80,000 units and 200,000 shares of common stock of Pacific Softworks by the security holders names below. Each unit consists of one share of common stock and one warrant. Each warrant entitles the holder to buy one share of common stock at a price of \$7.50 per share for a period of 24 months starting from the date of this prospectus. Pacific Softworks will not receive any of the proceeds of the sale of the securities by the selling security holders. Pacific Softworks will receive \$420,000 upon exercise of all the warrants to purchase units.

The following tables set forth information regarding the units and shares of common stock owned beneficially as of May \_\_\_\_, 1999 by each selling security holder. The selling security holders are not required, and may choose not, to sell any of their units or shares of common stock. The selling security holders have agreed with Spencer Edwards, Inc. not to sell any of their securities for a period of 13 months from the date of this prospectus without the prior written consent of the underwriter. None of the selling security holders is an officer, director or other affiliate of Pacific Softworks.

NAME OF SELLING UNIT HOLDER -----	UNITS OWNED PRIOR TO OFFERING -----	UNITS BEING OFFERED -----	UNITS AFTER OFFERING -----
Randall M. Gates	27,500	27,500	--
Georgette W. Pagano	12,500	12,500	--
Aaron A. Grunfeld	25,000	25,000	--
Ronald M. Resch	2,500	2,500	--
Lee M. Polster	2,500	2,500	--
Peter H. Alpert	2,500	2,500	--
Sheldon P. Berger	2,500	2,500	--
David Gitman	2,500	2,500	--
Nicolas Ramniceanu	2,500	2,500	--
	-----	-----	
Total	80,000	80,000	--
	=====	=====	

NAME OF SELLING STOCKHOLDER -----	SHARES OWNED PRIOR TO OFFERING -----	SHARES BEING OFFERED -----	SHARES AFTER OFFERING -----
John P. McGrain	140,000	140,000	--
Georgette W. Pagano	60,000	60,000	--
	-----	-----	
Total	200,000	200,000	--
	=====	=====	

## PLAN OF DISTRIBUTION

No underwriting arrangements exist as of the date of this prospectus for the selling security holders to sell their securities. Upon being advised of any underwriting arrangements that may be entered into by a selling security holder after the date of this prospectus, Pacific Softworks will prepare a supplement to this prospectus to disclose those arrangements. We anticipate that the selling price for the common stock and warrants will be at or between the "bid" and "asked" prices for these securities, as quoted in the over-the-counter market immediately preceding the sale.

To the extent that the selling security holders intend to sell their securities directly, through agents, dealers, or Spencer Edwards, Inc., in the over-the-counter market or otherwise, on terms and conditions that they determine at the time of sale or that they determine in private negotiations



between buyer and seller, their sales of the shares of common stock and warrants may be made in accordance with this prospectus and under the provisions of Rule 144 adopted under the Securities Act.

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PART II  
INFORMATION NOT REQUIRED IN PROSPECTUS

ITEM 24. INDEMNIFICATION OF DIRECTORS AND OFFICERS

Section 316 of the California General Corporation Law authorizes a court to award or a corporation's board of directors to grant indemnification to directors and officers in terms sufficiently broad to permit such indemnification under certain circumstances for liabilities (including reimbursement for expenses incurred) arising under the Securities Act of 1933. Article III Section 16 of the registrant's Bylaws provides for mandatory indemnification of its directors and officers and permissible indemnification of employees and other agents to the maximum extent permitted by the California General Corporation Law. The registrant's articles of incorporation provides that, pursuant to California law, its directors shall not be liable for monetary damages for breach of the directors' fiduciary duty as directors to the company and its stockholders. This provision in the articles of incorporation does not eliminate the directors' fiduciary duty, and in appropriate circumstances equitable remedies such as injunctive or other forms of non-monetary relief will remain available under California law. In addition, each director will continue to be subject to liability for breach of the director's duty of loyalty to Pacific Softworks for acts or omissions not in good faith or involving intentional misconduct, for knowing violations of law, for actions leading to improper personal benefit to the director, and for payment of dividends or approval of stock repurchases or redemptions that are unlawful under California law. The provision also does not affect a director's responsibilities under any other law, such as the federal securities laws or state or federal environmental laws. Pacific Softworks has entered into Indemnification Agreements with its officers and directors, a form of which is attached as Exhibit 10.1 hereto and incorporated herein by reference. The Indemnification Agreements provide the registrant's officers and directors with further indemnification to the maximum extent permitted by the California General Corporation Law. Reference is made to the Underwriting Agreement contained in Exhibit 1.1 hereto, which contains provisions indemnifying officers and directors of the registrant against certain liabilities.

ITEM 25. OTHER EXPENSES OF ISSUANCE AND DISTRIBUTION

The following table sets forth the costs and expenses, other than underwriting discounts, payable by Pacific Softworks in connection with the sale of units being registered. All amounts are estimates except the SEC registration fee, the NASD filing fee and the Nasdaq SmallCap Market listing fee.

SEC Registration fee .....	\$ 4,144
NASD fee .....	1,991
Nasdaq SmallCap Market listing fee.....	10,000
Printing and engraving expenses* .....	30,000
Legal fees and expenses* .....	60,000
Accounting fees and expenses* .....	40,000
Blue sky fees and expenses* .....	20,000
Transfer agent fees .....	1,825
Miscellaneous fees and expenses* .....	8,500
	-----
Total .....	\$176,460
	=====

\*Estimated

## ITEM 26. RECENT SALES OF UNREGISTERED SECURITIES

The following information relates to all securities sold within the past three years which were not registered under the Securities Act of 1933.

In February 1999 Pacific Softworks sold 100,000 units to a single accredited investor at a price of \$5.00 per unit for total proceeds of \$500,000. Each unit consisted of one share of common stock and one common stock purchase warrant entitling the holder of the warrant to purchase one share of common stock for two years at an exercise price of \$6.00 per share.

In February 1999 Pacific Softworks also sold and issued warrants to purchase 40,000 units to members of Resch Polster Alpert & Berger LLP, special counsel to Pacific Softworks in this offering, and warrants to purchase an additional 40,000 units to two persons who have provided temporary accounting and administrative services to Pacific Softworks. Each of these warrants to purchase units may be exercised at any time over a period of 60 months commencing from the date of this prospectus at a price of \$5.25. The units issuable upon exercise of these warrants are identical to the units sold in this offering.

Pacific Softworks issued these securities in reliance upon the exemption from registration provided by Section 4(2) of the Securities Act. The recipients of securities in these transactions represented their intention to acquire the securities for investment only and not with a view to or for sale in connection with any distribution thereof. The certificates evidencing the shares and warrants bear restrictive legends indicating that the shares and warrants were not registered under the Securities Act. No underwriter was involved in any of these transactions.

## ITEM 27. EXHIBITS

## (a) Exhibits

Exhibit No. -----	Description -----
1.1	Form of Underwriting Agreement
1.3	Form of Selected Dealers Agreement
3.1	Articles of Incorporation of the Registrant, as amended to date
3.2	Bylaws of the Registrant
4.2	Specimen Warrant
4.3	Form of Warrant Agreement
4.4	Specimen common stock certificate
4.5	Form of Lock Up Agreement
4.6	Form of Underwriter's Option for Purchase of Units
5.1	Opinion of Resch Polster Alpert & Berger LLP**
10.1	Form of Indemnification Agreements
10.2	1998 Equity Incentive Program
10.3	Security and Loan Agreement, dated September 15, 1998 between Bank of America National Trust and Savings Association and Pacific Softworks*
10.4	Form of Invention Assignment and Proprietary Information Agreement
10.5	Sublease, dated April 7, 1998 between SHR Perceptual Management and Pacific Softworks for the premises at 703 Rancho Conejo Blvd., Newbury Park, California*
10.6	Consulting Agreement dated March 8, 1996 between Kenneth Woodgrift and Pacific Softworks*
10.7	Letter from Pacific Softworks to Glenn Golenberg dated January 27, 1999 and Letter from Golenberg & Co, merchant bankers, to Glenn Russell dated June 18, 1998*
21.1	Subsidiary of the Registrant
23.1	Consent of Merdinger, Fruchter, Rosen & Corso, P.C., Independent Auditors

23.3	Consent of Counsel (contained within Exhibit 5.1)**
24.1	Power of Attorney (see page II-5)
27.1	Financial Data Schedule

\* Filed herewith.  
\*\* To be filed by amendment.

## (b) Financial Statement Schedules

All schedules have been omitted because the information required to be set forth therein is not applicable or is shown in the consolidated financial statements or notes thereto.

## ITEM 28. UNDERTAKINGS

The undersigned small business issuer will:

(1) File, during any period in which it offers or sells securities, a post-effective amendment to this registration statement to:

(i) Include any prospectus required by section 10(a)(3) of the Securities Act of 1933, as amended,

(ii) Reflect in the prospectus any facts or events which, individually or together, represent a fundamental change in the information in the registration statement, and

(iii) Include any additional or changed material information on the plan of distribution.

(2) For determining liability under the Securities Act, treat each post-effective amendment as a new registration statement of the securities offered, and the offering of the securities at that time to be the initial bona fide offering.

(3) File a post-effective amendment to remove from registration any of the securities that remain unsold at the end of the offering.

The small business issuer will provide to the underwriter at the closing specified in the underwriting agreement, certificates in such denominations and registered in such names as required by the underwriter to permit prompt delivery to each purchaser.

Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the small business issuer pursuant to the foregoing provisions, or otherwise, the small business issuer has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the small business issuer of expenses incurred or paid by a director, officer or controlling person of the small business issuer in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the small business issuer will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Securities Act and will be governed by the final adjudication of such issue.

The undersigned small business issuer will:

(1) For determining any liability under the Securities Act, treat the information omitted from the form of prospectus filed as part of this registration statement in reliance upon Rule 430A and contained in a form of prospectus filed by the small business issuer under Rule 424(b)(1), or (4) or 497(h) under the Securities Act as part of this registration statement as of the time the SEC declared it effective.

(2) For determining any liability under the Securities Act, treat each post-effective amendment that contains a form of prospectus as a new registration statement for the securities offered in the registration statement, and that offering of the securities at that time as the initial bona fide offering of those securities.

SIGNATURES

In accordance with the requirements of the Securities Act of 1933, as amended, the registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form SB-2 and authorized this registration statement to be signed on its behalf by the undersigned, in the city of Newbury Park, State of California, on this \_\_\_\_ day of May, 1999.

Pacific Softworks, Inc.

By /s/ Glenn P. Russell

-----  
Glenn P. Russell  
President and Chief Executive Officer



In accordance with the requirements of the Securities Act of 1933, as amended, this registration statement was signed by the following persons in the capacities and on the dates stated:

Signature -----	Title -----	Date -----
/s/ Glenn P. Russell ----- Glenn P. Russell	President, Chief Executive Officer and Chairman (Principal Executive Officer)	May 17, 1999
/s/ William E. Sliney ----- William E. Sliney	Chief Financial Officer (Principal Financial Officer)	May 17, 1999
/s/ Chaim Kaltgrad ----- Chaim Kaltgrad	Vice President	May 17, 1999
/s/ Mark Sewell* ----- Mark Sewell	Vice President	May 17, 1999
/s/ Sandra J. Garcia* ----- Sandra J. Garcia	Vice President	May 17, 1999
/s/ Robert G. J. Burg* ----- Robert G. J. Burg II	Director	May 17, 1999
/s/ Wayne T. Grau* ----- Wayne T. Grau	Director	May 17, 1999
/s/ Reuben Sandler* ----- Reuben Sandler, Ph.D.	Director	May 17, 1999

\* By Power of Attorney

## EXHIBIT INDEX

Exhibit No.	Description and Method of Filing
-----	-----
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24.1	Power of Attorney (see page II-5)
27.1	Financial Data Schedule

\* Filed herewith.

\*\* To be filed by amendment.

[BANK OF AMERICA LOGO]

TO: Bank of America National Trust  
and Savings Association  
UNIT NO. 1737  
141 MISSION FALLS LN  
FREMONT, CA 94539

BUSINESS LINE  
AGREEMENT - VARIABLE RATE  
SECURED BY PERSONAL PROPERTY

CUSTOMER NAME	LINE OF CREDIT NO.	CREDIT LIMIT
PACIFIC SOFTWARES, INC.	1718394-7002	\$250,000.00
BANKING OFFICE NO. CHECKING ACCOUNT NO. ("ACCOUNT")		
0174	01748-10498	

INTRODUCTION. This Agreement dated as of September 15, 1998 between PACIFIC SOFTWARES, INC. herein collectively and individually called "Borrower") and Bank of America National Trust and Savings Association (herein called "Bank") governs Borrower's Bank of America National Trust and Savings Association Business Line ("Line of Credit"). The words Borrower, "you" or "your" mean Borrower. The words "we," "us," or Bank, mean Bank. In consideration of, and to induce the Bank to make available to the Borrower the credit facility described herein, the Borrower agrees and warrants as follows:

#### I. THE LINE OF CREDIT

A. NATURE OF YOUR LINE OF CREDIT. Your Line of Credit is a revolving line of credit. This means that you, or any person provided for in I.C below, may request an advance of all or a part of your Line of Credit at any time prior to the Termination Date. By repaying any amount advanced, that amount becomes available to you as you need it unless (1) an Event of Default has occurred; (2) you exercise your right to cancel your Line of Credit; or (3) the Termination Date has occurred.

B. ADVANCES AND PAYMENTS. Advances under the Line of Credit may be in any amount not to exceed the credit limit remaining available.

C. TELEPHONE AUTHORIZATION. The Bank may honor telephone instructions for advances or repayments given by the individual signer(s) of this Agreement or a person or persons authorized by the signer(s) of this Agreement. Advances will be deposited in and repayments will be withdrawn from the Borrower's Account or such other accounts with the Bank as designated in writing by the Borrower. The Borrower indemnifies and excuses the Bank (including its officers, employees, and agents) from all liability, loss, and costs in connection with any act resulting from telephone instructions it reasonably believes are made by a signer of this Agreement or a person authorized by a signer. This indemnity and excuse will survive this Agreement's termination.

D. TERMINATION DATE. The term of the Line of Credit will expire on June 01, 1999 (the "Termination Date"), unless sooner terminated by the Bank pursuant to Section V herein, or canceled by you pursuant to Section I.M. On such date, no further advances will be available to Borrower and the entire outstanding principal balance of the line or Credit, together with all accrued and unpaid interest thereon, and fees and charges owing in connection therewith, shall be due and payable in full.

#### E. INTEREST RATE.

1. Unless modified in accordance with Section I.E.3, the outstanding principal amount of the Line of Credit shall bear interest at a fluctuating Interest Rate per annum equal to the Bank's Reference Rate plus 2.000 percentage points, as said Reference Rate may change from time to time.

The Reference Rate is the rate of interest publicly announced from time to time by the Bank in San Francisco, California as its Reference Rate. The Reference Rate is set by the Bank based on various factors, including the Bank's costs and desired return, general economic conditions and other factors, and is used as a reference point for pricing some loans. The Bank may price loans to its customers at, above, or below the Reference Rate. Any change in the Reference Rate shall take effect at the opening of business on the day specified in the public announcement of a change in the Bank's Reference Rate.

2. Computation of Interest and Fees. All computations of interest and fees made or called for hereunder shall be calculated on the basis of a 360 day year and the actual number of days elapsed. This results in more interest or a higher fee than if a 365 day year is used.

3. If, for any reason during the term of the line, the Automatic Repayment service mentioned in I.J.2. is terminated by the Borrower or the Bank, the Interest Rate on the line will increase by 1% (one percent), the amount of each payment will be increased accordingly, and the borrower agrees to pay a documentation fee of \$75.

4. At the Bank's sole option in each instance, any amount not paid when due under this Agreement (including interest) shall bear interest from the due date at the interest rate shown above in paragraph (1). This may result in compounding of interest.

F. SECURITY. As security for payment of this Line of Credit and all obligations provided for herein, you grant to us a security interest in the property described below. You also grant to us a security interest in all renewals of this property, other property substituted for it, and proceeds.

(1) ACCOUNTS REC & INVENTORY; (2) 0 VIN., MISC. EQUIP.

G. CREDIT LIMIT. A Credit Limit has been set on your Line of Credit and is shown above. As you use the Line of Credit, all advances will be deducted from your credit limit. You agree not to allow the principal amount which you owe us at any one time to exceed your credit limit. We do not have to honor any request for an advance which, when added to your unpaid principal balance, would exceed your credit limit.

H. PROMISE TO PAY. For value received, you promise to pay interest according to the terms of this Agreement, all advances outstanding including reasonable attorneys' fees, court costs, and collection costs.

I. FEES. Upon execution of this Agreement you will pay a nonrefundable Loan Fee of \_\_\_\_\_. You may pay by check, charge to your checking account or you may obtain an advance on your Line of Credit to pay these charges, and the advance will be subject to all the terms of this Agreement.

J. PAYMENTS.

1. The minimum payment due each month shall be interest, and shall be due and payable in full on the 10TH day of each month, or on the next business day if said date falls on a Saturday, Sunday, or Holiday for which the Bank is closed.

2. Borrower hereby chooses to have the interest payments made pursuant to the Bank's Automatic Repayment service, and authorizes Bank to collect all sums due hereunder by charging the Account the full amount thereof. Should there be insufficient funds in the Account to pay when due all or any portion of the interest due, the full amount of such deficiency shall be immediately due and payable by Borrower. All sums received from Borrower for application to the Line of Credit shall be applied first, to interest then due, second, to the outstanding principal balance and third, to any fees and charges outstanding. This applies to payments initiated by Borrower and to any sums collected by Bank by charges to the Account.

3. You can pay the outstanding balance on your Line of Credit in full or in part at any time without premium or penalty. We may accept partial payments, whether or not marked "paid in full" without losing our rights under this Agreement.

Principal and/or interest payments should be made to:

Bank of America National Trust and Savings Association  
Unit No. 1738  
PO BOX 6012  
PASADENA, CA 91102-6012

If we receive your payment by 9:00 a.m. on any banking day, we will credit your Line of Credit as of that day. You may make your payment at any of our banking offices.

K. CHANGE OF ADDRESS. You agree to notify us promptly in writing of a change in your mailing address.

L. LINES SECURED BY STOCKS/BONDS.

1. Margin Call. If at any time the credit limit to collateral value ratio exceeds 60% for lines secured partially or completely by stock, or 65% for lines secured only by bonds, we may send you notice requesting additional collateral. If the additional collateral is not received within the time given in the notice, you will be in default and we may terminate your Line of Credit as provided below.

2. Restrictions on Use of Funds. You agree not to use your Account to finance the purchase of margin stock (as defined by Regulation U) or to pay obligations incurred in the purchase of such securities.

M. CANCELLATION BY YOU. You may cancel this Agreement by written notice to the Bank. At the time of cancellation, the outstanding balance will be immediately due and payable.

N. CONDITIONS.

The Bank must receive the following items in form and content acceptable to the Bank before it is required to extend any credit to the Borrower under this Agreement.

A. AUTHORIZATIONS. Evidence that the execution, delivery and performance by the Borrower of this agreement and any instrument or agreement required under this agreement have been duly authorized.

B. GUARANTIES. Guaranties signed by those persons and in the amounts as required.

C. SECURITY AGREEMENTS. Signed original security agreements, deeds of

trust, financing statements and fixture filings (together with collateral in which the Bank requires a possessory security interest), which the Bank requires.

- D. Evidence of Priority. Evidence that security interests and liens in favor of the Bank are valid, enforceable, and prior to all others' rights and interests, except those the Bank consents to in writing.

### III. FINANCIAL STATEMENTS

- A. Borrower represents and warrants that Statements and data submitted in writing by Borrower to Bank in connection with this request for credit are true and correct, and said statements truly present the financial condition of Borrower as on the date thereof and the results of the operation of Borrower for the period covered thereby, and have been prepared in accordance with generally accepted accounting principles on a basis consistently maintained. Since such date, there have been no material adverse changes in the ordinary course of business. Borrower has no knowledge of any liabilities, contingent or otherwise, at such date not reflected in said statements, and Borrower has not entered into any special commitments or substantial contracts which are not reflected in said statements, other than in the ordinary and normal course of its business, which may have materially adverse effect upon its financial condition, operations or business as now conducted.
- B. The representation and warranty contained in Section A above shall apply to each financial statement submitted pursuant to Section IV.B herein and shall be continuous and shall be automatically restated for each such financial statement as of the date of such statement.

### IV. COVENANTS

Borrower agrees that so long as Bank may have any commitment to land or it is indebted to Bank, it will, unless Bank shall otherwise consent in writing:

- A. INSURANCE. Maintain public liability, property damage and worker's compensation insurance and insurance on all its insurable property against fire and other hazards with responsible insurance carriers to the extent usually maintained by similar businesses. If the Borrower fails to maintain insurance on the security described in Section I.F. herein, the Bank may, in its sole discretion, obtain such insurance and the cost of premiums shall be payable on demand with interest at the interest rate herein.

To maintain all risk property damage insurance policies covering the tangible property comprising the collateral. Each insurance policy must be in an amount acceptable to the Bank. The insurance must be issued by an insurance company acceptable to the Bank and must include a lender's loss payable endorsement in favor of the Bank in a form acceptable to the bank.

- B. RECORDS AND REPORTS. Maintain a standard and modern system of accounting in accordance with generally accepted accounting principles on a basis consistently maintained; permit Bank's representative to have access to and to examine its properties, books and records at all reasonable times; and furnish Bank: (1) promptly, a notice in writing of the occurrence of any event of default hereunder or of any event which would become an event of default hereunder upon giving of notice, lapse of time, or both, and (2) the following financial information and statements and such additional information as requested by the Bank from time to time; (a) by one year from the note date and annually thereafter, the Borrower's annual financial statements must be compiled by a Certified Public Accountant ("CPA") acceptable to the Bank; (b) by one year from the note date and annually thereafter, the Borrower's federal income tax return (with all forms K-1 attached), together with a statement of any contributions made by the Borrower to any subchapter S corporation or trust, and copies of any extensions of the filing date; (c) each guarantor's annual financial statements in form satisfactory to the Bank by one year from the note date and annually thereafter; and (d) copies of each guarantor's federal income tax return (with all forms K-1 attached) by one year from the note date and annually thereafter, together with a statement of any contributions made by the guarantor to any subchapter S corporation or trust, and copies of any extensions of the filing date.
- C. TYPE OF BUSINESS. Not make any substantial change in the character of its business.
- D. PURPOSE. Use the proceeds of this loan solely for business purposes.
- E. LOANS, SECONDARY LIABILITIES. Not make any loans or advances to any person or other entity other than in the ordinary and normal course of its business as now conducted; or guarantee or otherwise become liable upon the obligation of any person or other entity, except by endorsement of negotiable instruments for deposit or collection in the ordinary and normal course of its business.
- F. ACQUISITION OR SALE OF BUSINESS; MERGER OR CONSOLIDATION. Not purchase or otherwise acquire the assets or business of any person or other entity, or liquidate, dissolve, merge or consolidate, or commence any proceedings therefor, or sell any assets except in the ordinary and normal course of its business as now conducted, or sell, lease, assign, or transfer any substantial part of its business or fixed assets or any property or other assets necessary for the continuance of its business

as now conducted, including without limitation the selling of any property or other asset accompanied by the leasing back of the same.

- G. OUTSIDE INDEBTEDNESS. Not create, incur, assume or permit to exist any indebtedness for borrowed moneys other than loans from Bank except obligations now existing as shown in financial statements submitted pursuant to Section III.A herein; or sell or transfer, either with or without recourse, any accounts or notes receivable or any moneys due or to become due.
- H. COMPLIANCE WITH LAWS. Comply with the laws regulations and orders of any government body with authority over the Borrower's business.

V. EVENTS OF DEFAULT

The occurrence of any of the following events of default shall, at Bank's option, make all sums of principal and interest immediately due and payable, all without demand, presentment or notice, all of which are hereby expressly waived and the Bank may exercise all its rights against the Borrower, any guarantor and any collateral as provided by law.

- A. FAILURE TO PAY INDEBTEDNESS. Failure to pay any installment of interest on any indebtedness of Borrower to Bank.
- B. OTHER DEFAULTS. The occurrence of any event of default whether or not waived by the obligee under any other indebtedness extended by an institution or individual shall constitute an event of default hereunder.
- C. BREACH OF COVENANT. Failure of Borrower to perform any other term or condition of this agreement binding upon Borrower.
- D. BREACH OF WARRANTY. Any of Borrower's representations or warranties made herein or any statement or certificate at any time given in writing pursuant hereto or in connection herewith shall be false or misleading in any material respect.
- E. INSOLVENCY; RECEIVER OR TRUSTEE. Borrower, any guarantor of the indebtedness of Borrower to the Bank or general partner of Borrower shall become insolvent; or admit its inability to pay its debts as they mature; or make an assignment for the benefit of creditors; or apply for or consent to the appointment of a receiver or trustee for it or for a substantial part of its property of business.
- F. JUDGMENTS, ATTACHMENTS. Any money judgment, writ, or warrant of attachment, or similar process shall be entered or filed against Borrower or any of its assets and shall remain unvacated, unbonded or unstayed for a period of 10 days or in any event later than five days prior to the date of any proposed sale thereunder.
- G. BANKRUPTCY. Bankruptcy, insolvency, reorganization or liquidation proceedings, or other proceedings for relief under any bankruptcy law or any law for the relief of debtors shall be instituted by or against Borrower, any guarantor of the indebtedness of Borrower to the Bank or general partner of Borrower, and, if instituted against it, shall be consented to.
- H. DEFAULT IN SECURITY DOCUMENTS. A default shall occur in any document or instrument provided by the Borrower to the Bank in connection with the security provided the Bank pursuant to Paragraph I.F. herein.
- I. MATERIAL ADVERSE CHANGE. Should a material adverse change occur in Borrower's financial condition or the financial condition of any guarantor of the Borrower's obligations to Bank, which, in the opinion of the Bank, would affect the ability of the Borrower to repay the Borrower's obligations hereunder, or of such guarantor to perform under its guaranty.
- J. LOAN BALANCE. If the loan to collateral value reaches 100%.
- K. GUARANTY. Any guaranty of the indebtedness of the Borrower to the Bank, at any time after the execution and delivery of such guaranty and for any reason other than satisfaction in full of all indebtedness incurred hereunder, ceases to be in full force and effect or is declared to be null and void; or the validity or enforceability thereof is contested in a judicial proceeding; or any guarantor denies that it has any further liability under such guaranty, or should any guarantor default in any provision of any guaranty.
- L. LIEN PRIORITY. The Bank fails to have an enforceable first lien (except for any prior liens to which the Bank has consented in writing) on or security interest in any property given as security for this loan.
- M. DEATH. The Borrower or any guarantor dies (if the Borrower is a sole proprietorship, any owner dies; if the Borrower is a trust, a trustor dies; if the Borrower is a partnership, any general partner dies; or if the Borrower is a corporation, any principal officer or majority stockholder dies).
- N. GOVERNMENT ACTION. Any government authority takes action that the Bank believes materially adversely affects the Borrower's or any guarantor's financial condition or ability to repay.

If the Borrower is in default the Bank may also without prior notice, do any one or more of the following: (a) exercise any remedies available to a secured

party under the Uniform Commercial Code or any other applicable law; (b) proceed in the foreclosure of its security interest in the property described in the paragraph entitled "Security"; (c) sell or otherwise dispose of the property at public or private sale, upon terms and in such manner as it may determine and it may purchase same at such sale; (d) refrain from disposing of the property and continue to maintain possession of the property for such time as it deems appropriate, and Borrower takes the risk of any depreciation in the value of the property pending disposition; or (e) transfer any of the property into the name of Bank or Bank's nominee.

## VI. MISCELLANEOUS PROVISIONS

- A. **FAILURE OR INDULGENCE NOT WAIVER.** No failure or delay on the part of Bank, in the exercise of any power, right or privilege hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any such power, right or privilege preclude other or further exercise thereof or of any other right, power or privilege. All rights and remedies existing under this Agreement are cumulative to, and not exclusive of, any rights or remedies otherwise available.
- B. **OTHER AGREEMENTS.** Nothing herein shall in any way limit the effect of the conditions set forth in any security or other agreement executed by the Borrower, but each and every condition hereof shall be in addition thereto.
- C. **GOVERNING LAW.** This Agreement will be governed by the interpreted in accordance with the laws of the State of California.
- D. **SEVERABILITY.** If any provision of this Agreement is held to be unenforceable, such determination shall not affect the validity of the remaining provisions of the Agreement.
- E. **SUCCESSORS AND ASSIGNS.** This Agreement is binding on the Borrower's and the Bank's successors and assignees. The Borrower agrees that it may not assign this agreement without the Bank's prior consent.
- F. **ARBITRATION.**
1. This paragraph concerns the resolution of any controversies or claims between the Borrower and the Bank, including but not limited to those that arise from: (a) This Agreement (including any renewals, extensions or modifications of this Agreement); (b) Any document, agreement or procedure related to or delivered in connection with this Agreement; (c) Any violation of this Agreement; or (d) Any claims for, damages resulting from any business conducted between the Borrower and the Bank, including claims for injury to persons, property or business interests (torts).
  2. At the request of the Borrower or the Bank, any such controversies or claims will be settled by arbitration in accordance with the United States Arbitration Act. The United States Arbitration Act will apply even though this agreement provides that it is governed by California law.
  3. Arbitration proceedings will be administered by the American Arbitration Association and will be subject to its commercial rules of arbitration.
  4. For purposes of the application of the statute of limitations, the filing of an arbitration pursuant to this paragraph is the equivalent of the filing of a lawsuit, and any claim or controversy which may be arbitrated under this paragraph is subject to any applicable statute of limitations. The arbitrators will have the authority to decide whether any such claim or controversy is barred by the statute of limitations.
  5. If there is a dispute as to whether an issue is arbitrable, the arbitrators will have the authority to resolve any such dispute.
  6. The decision that results from an arbitration proceeding may be submitted to any authorized court of law to be confirmed and enforced.
  7. The procedure described above will not apply if the controversy or claim, at the time of the proposed submission to arbitration, arises from or relates to an obligation to the Bank secured by real property located in California. In this case, both the Borrower and the Bank must consent to submission of the claim or controversy to arbitration. If both parties do not consent to arbitration, the controversy or claim will be settled as follows: (a) The Borrower and the Bank will designate a referee (or panel of referees) selected under the auspices of the American Arbitration Association in the same manner as arbitrators are selected in Association-sponsored proceedings; (b) The designated referee (or panel of referees) will be appointed by a court as provided in California Code of Civil Procedures Section 638 and the following related sections; (c) The referee (or the presiding referee of the panel) will be an active attorney or a retired judge; and (d) The award that entered as a judgment in the court that appointed the referee, in accordance with the provisions of California Code of Civil Procedure Sections 644 and 645.
  8. This provision does not limit the right of the Borrower or the Bank to: (a) exercise self-help remedies such as setoff; (b) foreclose against or sell any real or personal property collateral or (c) act in a court of law, before, during or after the arbitrator proceeding to obtain (i) an interim remedy; and/or (ii) additional or supplementary remedies.
  9. The pursuit of or a successful action for interim, additional or supplementary remedies, or the filing of a court action, does not constitute a waiver of the right of the Borrower or the Bank, including the suing party, to submit the controversy or claim to arbitration if the other party contests the lawsuit. However, if the controversy or claim arises from or relates to an obligation to the Bank which is secured by real property located in California at the time of the proposed submission to arbitration, this right is limited according to the provision above requiring the consent of both the Borrower and the Bank to seek resolution through arbitration.
  10. If the Bank forecloses against any real property securing this Agreement, the Bank has the option to exercise the power of sale under the deed of trust or mortgage, or to proceed by judicial foreclosure.
- G. **HAZARDOUS WASTE INDEMNIFICATION.** The Borrower will indemnify and hold



harmless the Bank from any loss or liability directly or indirectly arising out of the use, generation, manufacture, production, storage, release, threatened release, discharge, disposal or presence of a hazardous substance. This Indemnity will apply whether the hazardous substance is on, under or about the Borrower's property or operations or property leased to the Borrower. The Indemnity includes but is not limited to attorney's fees (including the reasonable estimate of the allocated cost of in-house counsel and staff). The Indemnity extends to the Bank, its parent, subsidiaries and all of their directors, officers, employees, agents, successors, attorneys and assigns. For these purposes, the term "hazardous substances" means any substance which is or becomes designated as "hazardous" or "toxic" under any federal, state or local law. This Indemnity will survive repayment of the Borrower's obligations to the Bank.

- H. MULTIPLE BORROWERS. If two or more borrowers sign this agreement, each will be individually obligated to repay the Bank in full, and all will be obligated together.
- I. ONE AGREEMENT. This agreement and any related security or other agreements required by this Agreements, collectively: (1) represent the sum of the understandings and agreements between the Bank and the Borrower concerning this credit; and (2) replace any prior oral or written agreements between the Bank and the Borrower concerning this Agreement and any other agreements required by this Agreement, this Agreement and any other agreements required by this Agreement, this Agreement will prevail.
- J. NOTICE. As required herein, notice to the Bank shall be sent to the address shown on your latest billing statement, to be effective when received.

Notice to you shall be sent to you at your address in our records, to be effective when deposited in the U.S. mail, postage prepaid, unless otherwise stated in the notice.

This Agreement is executed as of the date stated at the top of the first page.

This Agreement is subject to a document entitled Addendum to Business Line Agreement dated September 15, 1998 attached and made a party thereof by this reference.

PACIFIC SOFTWARES, INC.

-----  
BY: -----  
GLENN RUSSELL, PRESIDENT

By: -----  
LAURA RUSSELL, SECRETARY

BUSINESS LOAN CONTINUING GUARANTY

in this guaranty, the guarantor refers to each business organization or person who signs below. The Bank refers to Bank of America National Trust and Savings Association.

1. GUARANTY

In consideration of the financial arrangements between the Bank and the borrowers listed below, the guarantor guarantees payment of, and agrees to pay to the order of the Bank, the debts to the Bank of:

PACIFIC SOFTWARES, INC.

BORROWER'S NAME

If there are two or more borrowers, the guarantor guarantees payment of any debt they incur together as well as debt each one incurs alone. The debt includes all obligations to the Bank the borrower incurs:

- at any time, past, present, or future;
- voluntarily or involuntarily;
- directly or indirectly; or
- individually or together with others.

The debt includes obligations;

- absolute or contingent;
- liquidated or unliquidated; or
- for a determined or undetermined amount.

This guaranty is continuous. Until revoked, it covers debts the borrower incurs even after fully repaying any previous debts. Each guarantor's obligations remain and will not be affected in the event of revocation by any other guarantor.

This guaranty is unconditional. The Bank may require the guarantor to pay even if the Bank does not:

- proceed against any borrower, guarantor, or other party;
- perfect any security interest;
- proceed against any security; or
- pursue any other remedy.

The Bank may release or add guarantors without releasing any other guarantor. The Bank may require the guarantor to pay even if a statute of limitations or disability bars recovery from the borrower, or the debt is or becomes otherwise unenforceable.

The guarantor waives the benefit of any statute of limitations that would apply to this guaranty.

The guarantor's obligations are independent of the borrower's obligations, and the Bank may sue the guarantor without suing the borrower.

2. LIMITS OF THE GUARANTY

At any one time, this guaranty is limited to:

- the principal amount of \$250,000.00; plus
- any interest, fees, and other expenses arising out of the debt, or the part of the debt covered by the limit of the principal amount.

The guarantor is not obligated for any amount over this limit, although the Bank may allow the borrower's debt to go above it.

The guarantor has the right to make a payment to the Bank on the debt and reduce the guaranty by that amount, but only if the Bank receives a written request to reduce the guaranty before or at the same time as the payment.

This guaranty is in addition to any other guaranty given by the guarantor.

If any borrower is a partnership and any guarantor is a general partner of that partnership, then such guarantor will not be liable under this guaranty for any debt of such borrower which is secured by real property; provided, however, that such guarantor will remain liable under partnership law for all debt of such borrower.

3. RIGHTS OF THE BANK

The Bank may from time to time, without notice to or demand on the guarantor:

- change the interest rate on or renew the debt;
- accelerate, extend, compromise, or otherwise change the repayment period of the debt;
- receive, substitute, or release collateral for the debt;

- - sell, otherwise dispose of, or apply collateral in any order;
- - apply amounts received from anyone other than the guarantor to any unguaranteed part of the debt;
- - assign or sell the whole or a portion of the debt and this guaranty; or
- - foreclose any deed of trust securing the debt, either by judicial foreclosure or power of sale. The guarantor understands and acknowledges that if the Bank forecloses, either by judicial foreclosure or by exercise of power of sale, any deed of trust securing the debt, that foreclosure could impair or destroy any ability that the guarantor may have to seek reimbursement, contribution or indemnification from the borrower or others based on any right the guarantor may have of subrogation, reimbursement, contribution or indemnification for any amounts paid by the guarantor under this guaranty. The guarantor further understands and acknowledges that in the absence of this paragraph, such potential impairment or destruction of the guarantor's rights, if any, may entitle the guarantor to assert a defense to this guaranty based on Section 580d of the California Code of Civil Procedure as interpreted in *Union Bank v. Gradsky*, 265 Cal.App.2d.40 (1968). By executing this guaranty, the guarantor freely, irrevocably and unconditionally: (i) waives and relinquishes that defense and agrees that the guarantor will be fully liable under this guaranty even though the Bank may foreclose, either by judicial foreclosure or by exercise of power of sale, any deed of trust securing the debt; (ii) agrees that the guarantor will not assert that defense in any action or proceeding which the Bank may commence to enforce this guaranty; (iii) acknowledges and agrees that the rights and defenses waived by the guarantor in this guaranty include any right or defense that the guarantor may have or be entitled to assert based upon or arising out of any one or more of Sections 580a, 580b, 580d, or 726 of the California Code of Civil Procedure or Section 2848 of the California Civil Code; and (iv) acknowledges and agrees that the Bank is relying on this waiver in creating the debt, and that this waiver is a material part of the consideration which the Bank is receiving for creating the debt.

The Bank may, at its option, request periodic financial statements from the guarantor. The guarantor agrees to supply these statements promptly, whenever they are requested.

The Bank may exercise these rights either before or after the guarantor revokes this guaranty, and without affecting any obligation under this guaranty.

The Bank may assign this guaranty, in whole or part, without notice, and the Bank and any assignee or purchaser, or any prospective assignee or purchaser of the debt, may exchange financial information about the guarantor with each other in connection with any assignment or purchase transaction.

If a borrower is a corporation or partnership, the Bank is not required to investigate the powers of anyone acting on the borrower's behalf.

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 4. PROTECTING THE BANK'S INTEREST  
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The guarantor agrees that any amounts the borrower owes the guarantor now or in the future are subordinated to the borrower's debt to the Bank. If the Bank requires, the guarantor, as a trustee for the Bank, will collect amounts the borrower owes the guarantor and pay them to the Bank in reduction of the debt to the Bank, without affecting or reducing any obligations under this guaranty.

- The guarantor agrees that the guarantor does not have any:
- - right of subrogation, reimbursement, indemnification or contribution arising from the existence or performance of this guaranty. This includes any such rights arising from contract, statutory law or otherwise, and includes any claim of subrogation under the Bankruptcy Code (Title 11 of the U.S. Code) or any successor statute;
  - - right to enforce a remedy which the Bank now has or may later have against the borrower;
  - - right to participate in security now or later held by the Bank; or
  - - right to any defense based on a claim that the obligations under this guaranty are more burdensome or are in excess of the borrower's debt to the Bank.

The guarantor is solely responsible for obtaining any financial information from the borrower the guarantor may require. The Bank is not required to give the guarantor any information about the borrower's business operations or financial condition, or any other notices or demands of any kind, including notices of new debts that may be incurred by the borrower, notices of default or notice of acceptance of this guaranty.

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 5. SECURITY AND RIGHT OF SETOFF  
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To secure all the debts covered by this guaranty, the guarantor assigns and grants to the Bank a security interest in all of the guarantor's:

- - money;
- - securities;
- - deposit accounts and their proceeds; and
- - any other property maintained in the possession of the Bank.

If the borrower defaults, or if any of the guarantor's obligations to the Bank are not fulfilled, the Bank may immediately use any money or proceeds of the guarantor's deposit accounts, securities, or other property in the Bank's possession to reduce the debt.

The Bank may also foreclose on any other collateral as provided in the Uniform Commercial Code and in any security agreements between the Bank and the guarantor.

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 6. ARBITRATION  
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This paragraph concerns the resolution of any controversies or claims between the guarantor and the Bank, including but not limited to those that arise from:

- (a) This guaranty (including any renewals, extensions or modifications of this guaranty);
- (b) Any document, agreement or procedure related to or delivered in connection with this guaranty;
- (c) Any violation of this guaranty; or
- (d) Any claims for damages resulting from any business conducted between the guarantor and the Bank, including claims for injury to persons, property or business interests (torts).

At the request of the guarantor or the Bank, any such controversies or claims will be settled by arbitration in accordance with the United States Arbitration Act. The United States Arbitration Act will apply even though this guaranty provides that it is governed by California law.

Arbitration proceedings will be administered by the American Arbitration Association and will be subject to its commercial rules of arbitration.

For purposes of the application of the statute of limitations, the filing of an arbitration pursuant to this paragraph is the equivalent of the filing of a lawsuit, and any claim or controversy which may be arbitrated under this paragraph is subject to any applicable statute of limitations. The arbitrators will have the authority to decide whether any such claim or controversy is barred by the statute of limitations and, if so, to dismiss the arbitration on that basis.

If there is a dispute as to whether an issue is arbitrable, the arbitrators will have the authority to resolve any such dispute.

The decision that results from an arbitration proceeding may be submitted to any authorized court of law to be confirmed and enforced.

The procedure described above will not apply if the controversy or claim, at the time of the proposed submission to arbitration, arises from or relates to an obligation to the Bank secured by real property located in California. In this case, both the guarantor and the Bank must consent to submission of the claim or controversy to arbitration. If both parties do not consent to arbitration, the controversy or claim will be settled as follows:

- (a) The guarantor and the Bank will designate a referee (or a panel of referees) selected under the auspices of the American Arbitration Association in the same manner as arbitrators are selected in Association-sponsored proceedings;
- (b) The designated referee (or the panel of referees) will be appointed by a court as provided in California Code of Civil Procedure Section 638 and the following related sections;
- (c) The referee (or the presiding referee of the panel) will be an active attorney or a retired judge; and
- (d) The award that results from the decision of the referee (or the panel) will be entered as a judgment in the court that appointed the referee, in accordance with the provisions of California Code of Civil Procedures Sections 644 and 645.

This provision does not limit the right of the guarantor or the Bank to:

- (a) exercise self-help remedies such as setoff;
- (b) foreclose against or sell any real or personal property collateral; or
- (c) act in a court of law, before, during or after the arbitration proceeding to obtain an interim remedy and/or additional or supplementary remedies.

The pursuit of or a successful action for interim, additional or supplementary remedies, or the filing of a court action, does not constitute a waiver of the right of the guarantor or the Bank, including the suing party, to submit the controversy or claim to arbitration if the other party contests the lawsuit. However, if the controversy or claim arises from or relates to an obligation to the Bank which is secured by real property located in California at the time of the proposed submission to arbitration, this right is limited according to the provision above requiring the consent of both the guarantor and the Bank to seek resolution through arbitration.

If the Bank forecloses against any real property securing this guaranty, the Bank has the option to exercise the power of sale under the deed of trust or

mortgage, or to proceed by judicial foreclosure.

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7. EXPENSES  
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The guarantor agrees to pay all reasonable attorneys' fees, including allocated costs of the Bank's in-house counsel, court costs and all other expenses the Bank incurs in enforcing this guaranty. The expenses covered by this provision include attorneys' fees and costs of any arbitration proceeding related to this guaranty.

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8. REVOKING THIS GUARANTY  
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The guarantor may revoke this guaranty as to future transactions at any time, provided the guarantor renounces any consideration given in return for the guaranty of such transactions. The guarantor is obligated on all credit extended by the Bank to the borrower until the Bank receives a written notice at the address shown below revoking the guaranty.

Any revocation will not affect the guarantor's obligation for any transactions that preceded receipt of the written notice, and the guarantor will remain obligated on all debts related to these transactions, even if those debts, before or after the revocation, have been renewed or modified or any of their terms have been changed in any way.

If this guaranty is revoked, cancelled or returned, and the Bank later must refund or rescind a payment, or transfer an interest in property back to the borrower, this guaranty will be reinstated as to that payment or interest.

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9. ENFORCING THIS GUARANTY  
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This guaranty is governed by California law, and the Bank may sue the guarantor in courts in California.

The Bank may delay or waive exercising or enforcing any of its rights, including its rights of setoff and lien, without losing them. These rights continue until the Bank waives them in writing.

If the guarantor is an individual and is married, or if an individual signing on behalf of a sole proprietorship or partnership is married, the Bank may proceed against his or her separate property for any obligations under this guaranty.

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10. SIGNATURES/DATE  
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All guarantors who sign are obligated individually and together under this guaranty. All guarantor signatures must be notarized if this guaranty is not signed in the presence of a Bank officer.

This document was prepared on September 15, 1998.

ADDRESS FOR NOTICES TO THE BANK:

Bank of America National Trust and Savings Association  
Unit No. 1737  
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THE RUSSELL TRUST DATED JUNE 23, 1997  
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\_\_\_\_\_  
09/15/98  
GLENN P. RUSSELL, TRUSTEE

\_\_\_\_\_  
09/15/98  
LAURA J. RUSSELL, TRUSTEE

CORPORATE RESOLUTION TO BORROW

Resolved that PACIFIC SOFTWARES, INC., a CALIFORNIA corporation, borrow from Bank of America National Trust and Savings Association.

1. BORROWING LIMIT

Resolved that at any one time the total borrowing authorized by this resolution is limited to the principal amount of \$250,000 plus any interest and fees.

The amount authorized by this resolution is in addition to any amounts authorized by any other resolution that has not been revoked.

2. AUTHORIZATION

Resolved that ANY ONE ACTING ALONE of the following officers (and their successors in office) may act for the corporation, including deciding how much and when to borrow.

1.	GLENN RUSSELL	PRESIDENT
	Name	Title
2.	LAURA RUSSELL	SECRETARY
	Name	Title
3.		
	Name	Title
4.		
	Name	Title

These officers are also authorized to:

- o sign and deliver to the Bank any documents evidencing the corporation's debt or any other agreements or documents the Bank may require and the officers approve;
- o request and agree to renewals or extensions;
- o grant a security interest in any property owned or controlled by the corporation as security for any borrowing under this resolution or other amounts the corporation owes the Bank;
- o apply for and obtain letters of credit; and
- o discount or sell security agreements, leases, bailment agreements, acceptances, drafts, receivables, notes and other evidences of debt to the Bank. These officers may endorse these documents in the corporation's name and guarantee payment.

3. REVOCATION

Resolved that the Bank is authorized to act on this resolution until notified in writing of its revocation.

4. SECRETARY'S CERTIFICATION

I, LAURA RUSSELL, the corporate secretary of the corporation named above, certify that this is an accurate copy of a resolution of its board of directors. The board adopted it as required by state law and the corporation's by-laws. It was adopted by a quorum of the board at a legal meeting of said Board duly and regularly held.

I also certify that this resolution is still in effect and has not been amended or revoked. The signatures below are those of the officers authorized to sign for this corporation by this resolution.

This certification was prepared on September 15, 1998.

5. SIGNATURES

Authorized Signatures:

-----  
GLENN RUSSELL

Signature

Print name

-----  
LAURA RUSSELL

Signature

Print name

-----  
Signature

Print name

-----  
Signature

Print name

-----  
Affix corporate seal here

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-----  
LAURA RUSSELL, SECRETARY  
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CORPORATE RESOLUTION TO SIGN GUARANTY

Resolved that LUKE SYSTEMS INTERNATIONAL a CALIFORNIA corporation, guarantee payment of the debt of PACIFIC SOFTWARES, INC. (the borrower) to Bank of America National Trust and Savings Association (the bank). Resolved that this corporation will receive a business benefit from the borrower's financial arrangements with the Bank and therefore will benefit from guaranteeing the debt.

1. BORROWING LIMIT

Resolved that at any one time the total borrowing authorized by this resolution is limited to the principal amount of \$250,000.00 plus any interest and fees. This amount is in addition to any other debt of the same borrower guaranteed under the authorization of separate resolutions.

2. AUTHORIZATION

Resolved that any ANY ONE ACTING ALONE of the officers named below (and their successors in office) are authorized to:

- \* sign the guaranty for the corporation;
\* grant a security interest in any property owned or controlled by the corporation as security for the guaranty; and
\* sign and deliver to the Bank any additional documents the Bank may require and the officers approve.

1. GLENN RUSSELL PRESIDENT
Name Title

2. GLENN RUSSELL SECRETARY
Name Title

3.
Name Title

4.
Name Title

3. REVOCATION

Resolved that the Bank is authorized to act on this resolution until notified in writing of its revocation.

4. SECRETARY'S CERTIFICATION

I, GLENN RUSSELL, the corporate secretary of the corporation named above, certify that this is an accurate copy of a resolution of its board of directors. The board adopted it as required by state law and the corporation's by-laws. It was adopted by a quorum of the board at a legal meeting of said Board duly and regularly held. I also certify that this resolution is still in effect and has not been amended or revoked. The signatures below are those of the officers authorized to sign for this corporation by this resolution. This certification was prepared on September 15, 1998.

5. SIGNATURES

Authorized Signatures:

Signature Print name GLENN RUSSELL
Signature Print name GLENN RUSSELL
Signature Print name
Signature Print name

Affix corporate seal here

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GLENN RUSSELL, SECRETARY  
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TRUST AUTHORITY LETTER

TO: Bank of America National Savings Association (the "Bank")

In accordance with California Probate Code Section 18100.5, the undersigned declare:

1. The undersigned, GLENN P. RUSSELL and LAURA J. RUSSELL (the "Trustees") are all of the duly appointed and acting trustees of the RUSSELL TRUST DATED JUNE 23, 1997 Trust (the "Trust").

2. The Trust is evidenced by that certain DECLARATION OF TRUST (the "Trust Agreement") executed on JUNE 23, 1997. The Trust Agreement is still in full force and effect and
[ ] has not been amended, altered, revoked or terminated in any way.
[ ] has been amended on the following dates: \_\_\_\_\_.

3. The trust is currently REVOCABLE.

4. [ ] (a) The Trustees have requested a \_\_\_\_\_ (the "Credit") from the Bank to the Trustees. This Credit will be secured by a security interest or deed of trust on \_\_\_\_\_ owned by the Trust.

[ ] (b) \_\_\_\_\_, trustor(s) of the Trust, have requested in their personal capacity a \_\_\_\_\_ (the "Credit") from the Bank. The Credit will be
[ ] secured by a security interest or deed of trust on \_\_\_\_\_ owned by the Trust.
[X] guaranteed by the Trust.

5. The Trustees are duly authorized under the terms of the Trust Agreement to enter into the transactions described above. The transactions are being entered into for a proper trust purpose.
[ ] The documentation for the transaction may be signed by any one of the Trustees, acting alone.

[X] (c) PACIFIC SOFTWARES, INC. has/have requested a Business Line (the "Credit") from the Bank. The Credit will be
[ ] secured by a security interest or deed of trust on \_\_\_\_\_
\_\_\_\_\_
owned by the Trust.
[X] guaranteed by the Trust.

6. Attached to this certificate are
[X] true and correct copies of the Trust Agreement and any amendments to the Trust Agreement.
[ ] true and correct copies of each portion of the Trust Agreement, and any amendments to the Trust Agreement, which designate the undersigned as trustees of the Trust and confer upon the Trustees the power to enter into the transactions described above.

7. We agree to immediately notify the Bank if:
(a) the Trust is revoked or terminated;
(b) the Trust is amended, in which case we agree to also provide the Bank with correct copies of the amendment(s);
(c) one or more trustee(s) change, in which case we also provide the Bank with signature exemplars of any new trustee(s);
(d) [X] or the Trust becomes irrevocable.

We understand that the occurrence of any of the events described in this paragraph may affect the right of the trustees of the Trust to incur further obligations or to further encumber the property. The Bank shall be authorized to continue to rely on this certificate until it receives notice as provided above. This agreement shall bind the Trustors, the current and successor trustees, and the current and successor beneficiaries.

Executed on September 15, 1998

Trustees: GLENN P. RUSSELL and LAURA J. RUSSELL

By \_\_\_\_\_
GLENN P. RUSSELL, TRUSTEE

By \_\_\_\_\_
LAURA J. RUSSELL, TRUSTEE

By \_\_\_\_\_

By \_\_\_\_\_

-----  
 SECURITY AGREEMENT:  
 RECEIVABLES, INVENTORY AND EQUIPMENT

TO: Bank of America National Trust and Savings Association

Unit No. 1737

-----  
 141 MISSION FALLS LN  
 -----

FREMONT, CA 94539  
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 1. THE SECURITY  
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The undersigned PACIFIC SOFTWARES, INC. ("Borrower") hereby assigns and grants to Bank of America National Trust and Savings Association ("Bank") a security interest in the following described property ("Collateral"):

- (a) The Collateral includes all of the following, whether now owned or hereafter acquired by Borrower: accounts, contract rights, chattel paper, instruments, deposit accounts, and general intangibles; and all returned or repossessed goods which, on sale or lease, resulted in an account or chattel paper.
- (b) The Collateral includes all inventory now owned or hereafter acquired by Borrower.
- (c) The Collateral includes all machinery, furniture, fixtures and other equipment of every type now owned or hereafter acquired by Borrower (including, but not limited to, the equipment described in the attached Equipment Description, if any).
- (d) All negotiable and nonnegotiable documents of title now owned or hereafter acquired by Borrower covering any of the above-described property.
- (e) All rights under contracts of insurance now owned or hereafter acquired by Borrower covering any of the above-described property.
- (f) All proceeds, product, rents and profits now owned or hereafter acquired by Borrower of any of the above-described property.
- (g) All books and records now owned or hereafter acquired by Borrower pertaining to any of the above-described property, including but not limited to any computer-readable memory and any computer hardware or software necessary to process such memory ("Books and Records").

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 2. THE INDEBTEDNESS  
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The Collateral secures and will secure all indebtedness of Borrower to Bank. For the purposes of this Agreement, "Indebtedness" means all loans and advances made by Bank to Borrower and all other obligations and liabilities of Borrower to Bank, whether now existing or hereafter incurred or created, whether voluntary or involuntary, whether due or not due, whether absolute or contingent, or whether incurred directly or acquired by Bank by assignment or otherwise. Unless Borrower shall have otherwise agreed in writing, indebtedness, for the purposes of this Agreement, shall not include "consumer credit" subject to the disclosure requirements of the Federal Truth in Lending Act or any regulations promulgated thereunder.

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 3. BORROWER'S COVENANTS  
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Borrower covenants and warrants that unless compliance is waived by Bank in writing:

- (a) Borrower will properly preserve the Collateral; defend the Collateral against any adverse claims and demands; and keep accurate Books and Records.
- (b) Borrower has notified Bank in writing of, and will notify Bank in writing prior to any change in, the locations of (i) Borrower's place of business or Borrower's chief executive office if Borrower has more than one place of business, and (ii) any Collateral, including the Books and Records.
- (c) Borrower will notify Bank in writing prior to any change in Borrower's name, identity or business structure.
- (d) Borrower will maintain and keep in force insurance covering Collateral designated by Bank against fire and extended coverages. Such insurance shall require losses to be paid on a replacement cost basis, be issued by insurance companies acceptable to Bank in a form acceptable to Bank.
- (e) Borrower has not granted and will not grant any security interest in any of the Collateral except to Bank, and will keep the Collateral

free of all liens, claims, security interests and encumbrances of any kind or nature except the security interest of Bank.

(f) Borrower will not sell, lease, agree to sell or lease, or otherwise dispose of, or remove from Borrower's place of business (i) any inventory except in the ordinary course of business as heretofore conducted by Borrower, or (ii) any other Collateral except with the prior written consent of Bank.

(g) Borrower will promptly notify Bank in writing of any event which affects the value of the Collateral, the ability of Borrower or Bank to dispose of the Collateral, or the rights and remedies of Bank in relation thereto, including, but not limited to, the levy of any legal process against any Collateral and the adoption of any marketing order, arrangement or procedure affecting the Collateral, whether governmental or otherwise.

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 (h) If any Collateral is or becomes the subject of any registration certificate or negotiable document of title, including any warehouse receipt or bill of lading, Borrower shall immediately deliver such document to Bank.

(i) Borrower will not attach any Collateral to any real property or fixture in a manner which might cause such Collateral to become a part thereof unless Borrower first obtains the written consent of any owner, holder of any lien on the real property or fixture, or other person having an interest in such property to the removal by Bank of the Collateral from such real property or fixture. Such written consent shall be in form and substance acceptable to Bank and shall provide that Bank has no liability to such owner, holder of any lien, or any other person.

(j) Until Bank exercises its rights to make collection, Borrower will diligently collect all Collateral.

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 4. ADDITIONAL OPTIONAL REQUIREMENTS  
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Borrower agrees that Bank may at its option at any time, whether or not Borrower is in default:

(a) Require Borrower to segregate all collections and proceeds of the Collateral so that they are capable of identification and deliver daily such collections and proceeds to Bank in kind.

(b) Require Borrower to deliver to Bank (i) copies of or extracts from the Books and Records, and (ii) information on any contracts or other matters affecting the Collateral.

(c) Examine the Collateral, including the Books and Records, and make copies of or extracts from the Books and Records, and for such purposes enter at any reasonable time upon the property where any Collateral or any Books and Records are located.

(d) Require Borrower to deliver to Bank any instruments or chattel paper.

(e) Require Borrower to obtain Bank's prior written consent to any sale, lease, agreement to sell or lease, or other disposition of any inventory.

(f) Notify any account debtors, any buyers of the Collateral, or any other persons of Bank's interest in the Collateral.

(g) Require Borrower to direct all account debtors to forward all payments and proceeds of the Collateral to a post office box under Bank's exclusive control.

(h) Demand and collect any payments and proceeds of the Collateral. In connection therewith Borrower irrevocably authorizes Bank to endorse or sign Borrower's name on all checks, drafts, collections, receipts and other documents, and to take possession of and open the mail addressed to Borrower and remove therefrom any payments and proceeds of the Collateral.

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 5. DEFAULTS  
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Any one or more of the following shall be a default hereunder:

(a) Borrower fails to pay any indebtedness when due.

(b) Borrower breaches any term, provision, warranty or representation under this Agreement, or under any other obligation of Borrower to Bank.

(c) Any custodian, receiver or trustee is appointed to take possession, custody or control of all or a substantial portion of the property of Borrower or of any guarantor of any indebtedness.

(d) Borrower or any guarantor of any indebtedness becomes insolvent, or is generally not paying or admits in writing its inability to pay its debts as they become due, fails in business, makes a general assignment for the benefit of creditors, dies or commences any case, proceeding or other action under any bankruptcy or other law for the relief of, or relating to, debtors.

(e) Any case, proceeding or other action is commenced against Borrower or any guarantor of any indebtedness under any bankruptcy or other law for the relief of, or relating to, debtors.

(f) Any involuntary lien of any kind or character attaches to any Collateral.

(g) Any financial statements, certificates, schedules or other information now or hereafter furnished by Borrower to Bank proves false or incorrect in any material respect.

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 6. BANK'S REMEDIES AFTER DEFAULT  
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In the event of any default Bank may do any one or more of the following:

(a) Declare any indebtedness immediately due and payable, without notice or demand.

(b) Enforce the security interest given hereunder pursuant to the Uniform Commercial Code and any other applicable law.

(c) Enforce the security interest of Bank in any deposit account of Borrower maintained with Bank by applying such account to the indebtedness.

(d) Require Borrower to assemble the Collateral, including the Books and Records, and make them available to Bank at a place designated by Bank.

(e) Enter upon the property where any Collateral, including any books and Records, are located and take possession of such Collateral and such Books and Records, and use such property (including any buildings and facilities) and any of Borrower's equipment, if Bank deems such use necessary or advisable in order to take possession of, hold, preserve, process, assemble, prepare for sale or lease, market for sale or lease, sell or lease, or otherwise dispose of, any Collateral.

(f) Grant extensions and compromise or settle claims with respect to the Collateral for less than face value, all without prior notice to Borrower.

(g) Use or transfer any of Borrower's rights and interests in any Intellectual Property now owned or hereafter acquired by Borrower, if Bank deems such use necessary or advisable in order to take possession of, hold, preserve, process, assemble, prepare for sale or lease, market for sale or lease, sell or lease, or otherwise dispose of, any Collateral. Borrower agrees that any such use or transfer shall be without any additional consideration to Borrower. As used in this paragraph, "Intellectual Property" includes, but is not limited to, all trade secrets, computer software, service marks, trademarks, trade names, trade styles, copyrights, patents, applications for any of the foregoing, customer lists, working drawings, instructional manuals, and rights in processes for technical manufacturing, packaging and labelling, in which Borrower has any right or interest, whether by ownership, license, contract or otherwise.

(h) Have a receiver appointed by any court of competent jurisdiction to take possession of the Collateral.

(i) Take such measures as Bank may deem necessary or advisable to take possession of, hold, preserve, process, or lease, sell or lease, or otherwise dispose of, any Collateral, and Borrower hereby irrevocably constitutes and appoints Bank as Borrower's attorney-in-fact to perform all acts and execute all documents in connection therewith.

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7. MISCELLANEOUS  
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(a) Any waiver, express or implied, of any provision hereunder and any delay or failure by Bank to enforce any provision shall not preclude Bank from enforcing any such provision thereafter.

(b) Borrower shall, at the request of Bank, execute such other agreements, documents, instruments, or financing statements in connection with this Agreement as Bank may reasonably deem necessary.

(c) All notes, security agreements, subordination agreements and other documents executed by Borrower or furnished to Bank in connection with this Agreement must be in form and substance satisfactory to Bank.

(d) This Agreement shall be governed by and construed according to the laws of the State of California, to the jurisdiction of which the parties hereto submit.

(e) All rights and remedies herein provided are cumulative and not exclusive of any rights or remedies otherwise provided by law. Any single or partial exercise of any right or remedy shall not preclude the further exercise thereof or the exercise of any other right or remedy.

(f) All terms not defined herein are used as set forth in the Uniform Commercial Code.

(g) In the event of any action by Bank to enforce this Agreement or to protect the security interest of Bank in the Collateral, or to take possession of, hold, preserve, process, assemble, prepare for sale or lease, market for sale or lease, sell or lease, or otherwise dispose of, any Collateral, Borrower agrees to pay immediately the costs and expenses thereof, together with reasonable attorney's fees and allocated costs for in-house legal services.

(h) Any Borrower who is married agrees that such Borrower's separate property shall be liable for payment of the Indebtedness if such Borrower is personally liable for the Indebtedness.

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8. SIGNATURES/DATE  
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This document was prepared on September 15, 1998.

PACIFIC SOFTWARES, INC.  
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By \_\_\_\_\_  
GLENN RUSSELL, PRESIDENT

By \_\_\_\_\_  
LAURA RUSSELL, SECRETARY



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AUTHORIZATION FOR DISBURSEMENT OF LOAN PROCEEDS

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION  
 BUSINESS LENDING SERVICES Date September 15, 1998

The BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION BUSINESS LENDING SERVICES is authorized to disburse the proceeds of that certain note dated September 15, 1998 in the amount of \$250,000.00 executed by the undersigned, as follows:

Pay by cashiers check to	No.	\$0.00
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Pay by cashiers check to	No.	\$0.00
-----	-----	-----
Pay by purchase draft to	No.	\$0.00
-----	-----	-----
Credit Account	No.	\$0.00
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Credit Account	No.	\$0.00
-----	-----	-----
Renew Loan No. 7002	Remainder Undisbursed	\$250,000.00
-----	-----	-----
Payoff Loan No.	As of:	\$0.00
-----	-----	-----
Undisbursed		\$0.00
-----		-----
Other		\$0.00
-----		-----
Fees	Financed Fees	\$0.00
-----	-----	-----
	TOTAL:	\$250,000.00
		-----

Collect interest in the amount of \_\_\_\_\_ to \_\_\_\_\_

Borrower hereby authorizes the Bank to deduct from loan proceeds any uncollected fees and any uncollected interest due from the Borrower to the Bank.

1718394-7002  
 -----  
 PACIFIC SOFTWARES, INC.  
 -----  
 By \_\_\_\_\_  
 GLENN RUSSELL, PRESIDENT  
 By \_\_\_\_\_  
 LAURA RUSSELL, SECRETARY

Breakdown of fees are as follows:

Loan fee:	-----
Doc fee:	-----
Setup fee:	-----
	-----
	-----
Inspection fee:	-----
Appraisal fee:	-----
Escrow fee:	-----
Title fee:	-----
Lot book fee:	-----
Recording fee:	-----
Extension fee:	-----
Credit report fee:	-----
UCC filings fee:	-----
service fee:	-----
Credit Life Ins fee:	-----
TOTAL FEES:	\$0.00
	-----

[BANK OF AMERICA LOGO]

ADDENDUM TO BUSINESS LINE AGREEMENT  
FEES/DEFAULT RATE

This Addendum dated September 15, 1998 is part of the Business Line Agreement between PACIFIC SOFTWARES, INC. ("Borrower") and BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION ("Bank") dated September 15, 1998 (the "Agreement").

The Borrower agrees, so long as credit is available under the Agreement, and until the Bank is repaid in full:

I. FEES

(a) STATEMENT COPY FEE. A fee may be charged for each statement copy requested, plus an hourly charge for any necessary research time.

(b) LATE FEE. If payment is not received within 15 days after the date the payment is due, a late charge of 6% of the unpaid portion of the payment amount, with a minimum of \$5 and a maximum of \$15 may be assessed. This fee may be changed by the Bank at its option.

(c) OVERLIMIT FEE. An overlimit fee of \$15 may be assessed each time the Borrower exceeds the Credit Limit, regardless of whether the Bank permits the Borrower to exceed the Credit Limit.

(d) RETURNED ITEM FEE. The Borrower may be charged a returned item fee of \$10 each time a payment is returned or if there are insufficient funds in the Checking Account when a payment is attempted through Automatic Payment Service.

II. DEFAULT RATE.

Upon the occurrence and during the continuation of any default under the Agreement, amounts outstanding under the Agreement will at the option of the Bank bear interest at a rate per annum which is \_\_\_\_\_ (\_\_\_\_\_) percentage points higher than the rate of interest otherwise provided under the Agreement. This will not constitute a waiver of any default.

III. OTHER.

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PACIFIC SOFTWARES, INC.

By \_\_\_\_\_  
GLENN RUSSELL, PRESIDENT

By \_\_\_\_\_  
LAURA RUSSELL, SECRETARY

By \_\_\_\_\_

By \_\_\_\_\_

GLENN P. RUSSELL and LAURA J. RUSSELL, Trustor(s) of the RUSSELL TRUST DATED JUNE 23, 1997 (the "Trust"), established pursuant to that certain Declaration of Trust/Trust Agreement dated JUNE 23, 1997 and amended on \_\_\_\_\_ (the "Trust Agreement") hereby declare that:

- 1. They are the Trustor(s) of the Trust;
- 2. They have retained the power to amend or revoke the Trust pursuant to the terms of the Trust Agreement;
- 3. They have the power pursuant to Section 16001 of the California Probate Code to direct the Trustee(s) of the Trust to take such actions as the Trustor(s) shall desire;
- 4. They hereby direct the Trustee(s) of the Trust to:

[ ] encumber the following trust assets to secure the indebtedness of

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to Bank of America National Trust and Savings Association:

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[X] execute a continuing guaranty in favor of Bank of America National Trust and Savings Association in the principal amount of \$250,000.00 guaranteeing the indebtedness of PACIFIC SOFTWORKS, INC.

- 5. The Trustee(s) shall incur no liability to any person having a vested or contingent interest in the Trust as a result of following the directions contained herein.

The undersigned acknowledge that a copy of this letter will be delivered to Bank as evidence of the Trustee(s)' authority to enter in the transaction described above.

Date: September 15, 1998  
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GLENN P. RUSSELL, TRUSTOR OF THE  
RUSSELL TRUST DATED JUNE 23, 1997

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LAURA J. RUSSELL, TRUSTOR OF THE  
RUSSELL TRUST DATED JUNE 23, 1997

## [AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION LOGO]

STANDARD SUBLEASE  
(LONG-FORM TO BE USED WITH PRE-1996 AIR LEASES)

1. PARTIES. This Sublease, dated, for reference purposes only, April 7, 1998, is made by and between SHR Perceptual Management, an Arizona Corporation ("SUBLESSOR") and Pacific Softworks, Inc., a California Corporation ("SUBLESSEE").

2. PREMISES. Sublessor hereby subleases to Sublessee and Sublessee hereby subleases from Sublessor for the term, at the rental, and upon all of the conditions set forth herein, that certain real property, including all improvements therein, and commonly known by the street address of 703 Rancho Conejo Blvd., Newbury Park, California located in the County of Ventura, State of California and generally described as (describe briefly the nature of the property) an approximate 11,468 square foot concrete tilt-up industrial building situated on approximately 31,588 square feet of land zoned M1 and to include thirty (30) reserved car parking spaces. See Exhibit A attached. ("PREMISES").

## 3. TERM.

3.1 TERM. The term of this Sublease shall be for twenty-nine and one-half (29-1/2) months commencing on May 1, 1998 and ending on September 15, 2000 unless sooner terminated pursuant to any provision hereof.

3.2 DELAY IN COMMENCEMENT. Sublessor agrees to use its best commercially reasonable efforts to deliver possession of the Premises by the commencement date. If, despite said efforts, Sublessor is unable to deliver possession as agreed, Sublessor shall not be subject to any liability therefor, nor shall such failure affect the validity of this Sublease. Sublessee shall not, however, be obligated to pay Rent or perform its other obligations until it receives possession of the Premises. If possession is not delivered within sixty days after the commencement date, Sublessee may, at its option, by notice in writing within ten days after the end of such sixty day period, cancel this Sublease, in which event the Parties shall be discharged from all obligations hereunder. If such written notice is not received by Sublessor within said ten day period, Sublessee's right to cancel shall terminate. Except as otherwise provided, if possession is not tendered to Sublessee when required and Sublessee does not terminate this Sublease, as aforesaid, any period of rent abatement that Sublessee would otherwise have enjoyed shall run from the date of delivery of possession and continue for a period equal to what Sublessee would otherwise have enjoyed under the terms hereof, but minus any days of delay caused by the acts or omissions of Sublessee. If possession is not delivered within 120 days after the commencement date, this Sublease shall automatically terminate unless the Parties agree, in writing, to the contrary.

## 4. RENT.

4.1 BASE RENT. Sublessee shall pay to Sublessor as Base Rent for the Premises equal monthly payments of \$8,486.32 in advance, on the first day of each month of the term hereof. Sublessee shall pay Sublessor upon the execution hereof \$8,486.32 as Base Rent for month of May 1998. Base Rent for any period during the term hereof which is for less than one month shall be a pro rata portion of the monthly installment.

4.2 RENT DEFINED. All monetary obligations of Sublessee to Sublessor under the terms of this Sublease (except for the Security Deposit) are deemed to be rent ("Rent"). Rent shall be payable in lawful money of the United States to Sublessor at the address stated herein or to such other persons or at such other places as Sublessor may designate in writing.

5. SECURITY DEPOSIT. Sublessee shall deposit with Sublessor upon execution hereof \$8,486.32 as security for Sublessee's faithful performance of Sublessee's obligations hereunder. If Sublessee fails to pay Rent or other charges due hereunder, or otherwise defaults with respect to any provision of this Sublease, Sublessor may use, apply or retain all or any portion of said deposit for the payment of any Rent or other charge in default or for the payment of any other sum to which Sublessor may become obligated by reason of Sublessee's default, or to compensate Sublessor for any loss or damage which Sublessor may suffer thereby. If Sublessor so uses or applies all or any portion of said deposit, Sublessee shall within ten days after written demand therefore forward to Sublessor an amount sufficient to restore said Deposit to the full amount provided for herein and Sublessee's failure to do so shall be a material breach of this Sublease. Sublessor shall not be required to keep said Deposit separate from its general accounts. If Sublessee performs all of Sublessee's obligations hereunder, said Deposit, or so much thereof as has not therefore been applied by Sublessor, shall be returned, without payment of interest to Sublessee (or at Sublessor's option, to the last assignee, if any, of Sublessee's interest hereunder) at the expiration of the term hereof, and after Sublessee has vacated the Premises. No trust relationship is created herein between Sublessor and Sublessee with respect to said Security Deposit.

## 6. USE.

6.1 AGREED USE. The Premises shall be used and occupied only for software development, general office and other lawful related uses, and for no other purpose.

6.2 COMPLIANCE. Sublessor warrants that the improvements on the Premises comply with all applicable covenants or restrictions of record and applicable building codes, regulations and ordinances ("APPLICABLE

REQUIREMENTS") in effect on the commencement date. Said warranty does not apply to the use to which Sublessee will put the Premises or to any alterations or utility installations made or to be made by Sublessee. NOTE: Sublessee is responsible for determining whether or not the zoning is appropriate for its intended use, and acknowledges that past uses of the Premises may no longer be allowed. If the Premises do not comply with said warranty, Sublessor shall, except as otherwise provided, promptly after receipt of written notice from Sublessee setting forth with specificity the nature and extent of such non-compliance, rectify the same at Sublessor's expense. If Sublessee does not give Sublessor written notice of a non-compliance with this warranty within six months following the commencement date, correction of that non-compliance shall be the obligation of Sublessee at its sole cost and expense. If the Applicable Requirements are hereafter changed so as to require during the term of this Sublease 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"). Sublessor and Sublessee shall allocate the cost of such work as follows:

(a) If such Capital Expenditures are required as a result of the specific and unique use of the Premises by Sublessee as compared with uses by tenants in general, Sublessee shall be fully responsible for the cost thereof provided, however, that if such Capital Expenditure is required during the last two years of this Sublease and the cost thereof exceeds six months' Base Rent, Sublessee may instead terminate this Sublease unless Sublessor notifies Sublessee in writing, within ten days after receipt of Sublessee's termination notice that Sublessor has elected to pay the difference between the actual cost thereof and the amount equal to six months' Base Rent. If the Parties elect termination, Sublessee shall immediately cease the use of the Premises which requires such Capital Expenditure and deliver to Sublessor written notice specifying a termination date at least ninety days thereafter. Such termination date shall, however, in no event be earlier than the last day that Sublessee 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 Sublessee (such as governmentally mandated seismic modifications, then Sublessor shall pay for said Capital Expenditure and the cost thereof shall be prorated between the Sublessor and Sublessee and Sublessee shall only be obligated to pay, each month during the remainder of the term of this Sublease, on the date on which Rent is due, an amount equal to the product of multiplying the cost of such Capital Expenditure 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 Capital Expenditure 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 Sublessor's accountant), with Sublessee reserving the right to prepay its obligation at any time. Provided, however, that if such Capital Expenditure is required during the last two years of this Sublease or if Sublessor reasonably determines that it is not economically feasible to pay its share thereof, Sublessor shall have the option to terminate this Sublease upon ninety days prior written notice to Sublessee unless Sublessee notifies Sublessor, in writing, within ten days after receipt of Sublessor's termination notice that Sublessee will pay for such Capital Expenditure. If Sublessor does not elect to terminate, and fails to tender its share of any such Capital Expenditure, Sublessee may advance such funds and deduct same, with interest, from Rent until Sublessor's share of such costs have been fully paid. If Sublessee is unable to finance Sublessor's share, or if the balance of the Rent due and payable for the remainder of this Sublease is not sufficient to fully reimburse Sublessee on an offset basis, Sublessee shall have the right to terminate this Sublease upon ten days written notice to Sublessor.

(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 Sublessee 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, Sublessee shall be fully responsible for the cost thereof, and Sublessee shall not have any right to terminate this Sublease.

#### 6.3 ACCEPTANCE OF PREMISES AND LESSEE. Sublessee acknowledges that:

(a) it has been advised by Brokers to satisfy itself with respect to the condition of the Premises (including but not limited to the electrical, HVAC and fire sprinkler systems, security, environmental aspects, and compliance with Applicable Requirements), and their suitability for Sublessee's intended use,

(b) Sublessee has made such investigation as it deems necessary with reference to such matters and assumes all responsibility therefor as the same relate to its occupancy of the Premises, and

(c) neither Sublessor, Sublessor's agents, nor any Broker has made any oral or written representations or warranties with respect to said matters other than as set forth in this Sublease.

In addition, Sublessor acknowledges that:

(a) Broker has made no representations, promises or warranties concerning Sublessee's ability to honor the Sublease or suitability to occupy the Premises, and

(b) it is Sublessor's sole responsibility to investigate the financial capability and/or suitability of all proposed tenants.

#### 7. MASTER LEASE

7.1 Sublessor is the lessee of the Premises by virtue of a lease, hereinafter the "MASTER LEASE", a copy of which is attached hereto marked Exhibit 1, wherein Frank D. McDonald, dba Rancho Conejo Properties is the lessor, hereinafter the "MASTER LESSOR".

7.2 This Sublease is and shall be at all times subject and subordinate to the Master Lease.

7.3 The terms, conditions and respective obligations of Sublessor and Sublessee to each other under this Sublease shall be the terms and conditions of the Master Lease except for those provisions of the Master Lease which are directly contradicted by this Sublease in which event the terms of this Sublease document shall control over the Master Lease. Therefore, for the purposes of this Sublease, wherever in the Master Lease the word "Lessor" is used it shall be deemed to mean the Sublessor herein and wherever in the Master Lease the word "Lessee" is used it shall be deemed to mean the Sublessee herein.

7.4 During the term of this Sublease and for all periods subsequent for obligations which have arisen prior to the termination of this Sublease,

Sublessee does hereby expressly assume and agree to perform and comply with, for the benefit of Sublessor and Master Lessor, each and every obligation of Sublessor under the Master Lease except for the following paragraphs which are excluded therefrom:

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7.5 The obligations that Sublessee has assumed under paragraph 7.4 hereof are hereinafter referred to as the "SUBLESSEE'S ASSUMED OBLIGATIONS". The obligations that sublessee has not assumed under paragraph 7.4 hereof are hereinafter referred to as the "SUBLESSOR'S REMAINING OBLIGATIONS".

7.6 Sublessee shall hold Sublessor free and harmless from all liability, judgments, costs, damages, claims or demands, including reasonable attorneys fees, arising out of Sublessee's failure to comply with or perform Sublessee's Assumed Obligations.

7.7 Sublessor agrees to maintain the Master Lease during the entire term of this Sublease, subject, however, to any earlier termination of the Master Lease without the fault of the Sublessor, and to comply with or perform Sublessor's Remaining Obligations and to hold Sublessee free and harmless from all liability, judgments, costs, damages, claims or demands arising out of Sublessor's failure to comply with or perform Sublessor's Remaining Obligations.

7.8 Sublessor represents to Sublessee that the Master Lease is in full force and effect and that no default exists on the part of any Party to the Master Lease.

#### 8. ASSIGNMENT OF SUBLEASE AND DEFAULT.

8.1 Sublessor hereby assigns and transfers to Master Lessor the Sublessor's interest in this Sublease, subject however to the provisions of Paragraph 8.2 hereof.

8.2 Master Lessor, by executing this document, agrees that until a Default shall occur in the performance of Sublessor's Obligations under the Master Lease, that Sublessor may receive, collect and enjoy the Rent accruing under this Sublease. However, if Sublessor shall Default in the performance of its obligations to Master Lessor then Master Lessor may, at its option, receive and collect, directly from Sublessee, all Rent owing and to be owed under this Sublease. Master Lessor shall not, by reason of this assignment of the Sublease nor by reason of the collection of the Rent from the Sublessee, be deemed liable to Sublessee for any failure of the Sublessor to perform and comply with Sublessor's Remaining Obligations.

8.3 Sublessor hereby irrevocably authorizes and directs Sublessee upon receipt of any written notice from the Master Lessor stating that a Default exists in the performance of Sublessor's obligations under the Master Lease, to pay to Master Lessor the Rent due and to become due under the Sublease. Sublessor agrees that Sublessee shall have the right to rely upon any such statement and request from Master Lessor, and that Sublessee shall pay such Rent to Master Lessor without any obligation or right to inquire as to whether such Default exists and notwithstanding any notice from or claim from Sublessor to the contrary and Sublessor shall have no right or claim against Sublessee for any such Rent so paid by Sublessee.

8.4 No charges or modifications shall be made in this Sublease without the consent of Master Lessor.

#### 9. CONSENT OF MASTER LESSOR.

9.1 In the event that the Master Lease requires that Sublessor obtain the consent of Master Lessor to any subletting by Sublessor then, this Sublease shall not be effective unless, within ten days of the date hereof, Master Lessor signs this Sublease thereby giving its consent to this Subletting.

9.2 In the event that the obligations of the Sublessor under the Master Lease have been guaranteed by third parties then neither this Sublease, nor the Master Lessor's consent, shall be effective unless, within 10 days of the date hereof, said guarantors sign this Sublease thereby giving their consent to this Sublease.

9.3 In the event that Master Lessor does give such consent then:

(a) Such consent shall not release Sublessor of its obligations or alter the primary liability of Sublessor to pay the Rent and perform and comply with all of the obligations of Sublessor to be performed under the Master Lease.

(b) The acceptance of Rent by Master Lessor from Sublessee or anyone else liable under the Master Lease shall not be deemed a waiver by Master Lessor of any provisions of the Master Lease.

(c) The consent to this Sublease shall not constitute a consent to any subsequent subletting or assignment.

(d) In the event of any Default of Sublessor under the Master Lease, Master Lessor may proceed directly against Sublessor, any guarantors or anyone else liable under the Master Lease or this Sublease without first exhausting Master Lessor's remedies against any other person or entity liable thereon to Master Lessor.

(e) Master Lessor may consent to subsequent sublettings and assignments of the Master Lease or this Sublease or any amendments or modifications thereto without notifying Sublessor or anyone else liable under the Master Lease and without obtaining their consent and such action shall not relieve such persons from liability.

(f) In the event that Sublessor shall Default in its obligations under the Master Lease, then Master Lessor, at its option and without being obligated to do so, may require Sublessee to attorn to Master Lessor in which event Master Lessor shall undertake the obligations of Sublessor under this Sublease from the time of the exercise of said option to termination of this Sublease but Master Lessor shall not be liable for any prepaid Rent nor any Security Deposit paid by Sublessee, nor shall Master Lessor be liable for any other Defaults of the Sublessor under the Sublease.

9.4 The signature of the Master Lessor and any Guarantors of Sublessor at the end of this document shall constitute their consent to the terms of this Sublease.

9.5 Master Lessor acknowledges that, to the best of Master Lessor's knowledge, no Default presently exists under the Master Lease of obligations to be performed by Sublessor and that the Master Lease is in full force and effect.

9.6 In the event that Sublessor Defaults under its obligations to be performed under the Master Lease by Sublessor, Master Lessor agrees to deliver to Sublessee a copy of any such notice of default. Sublessee shall have the right to cure any Default of Sublessor described in any notice of default within ten days after service of such notice of default on Sublessee. If such Default is cured by Sublessee then Sublessee shall have the right of reimbursement and offset from and against Sublessor.

#### 10. BROKERS FEE.

10.1 Upon execution hereof by all parties, Sublessor shall pay to CB Commercial Real Estate Group, Inc. a licensed real estate broker, ("BROKER"), a fee as set forth in a separate agreement between Sublessor and Broker, for brokerage services rendered by Broker to Sublessor in this transaction.

10.2 Sublessor agrees that if Sublessee exercises any option or right of first refusal as granted by Sublessor herein, or any option or right substantially similar thereto, either to extend the terms of this Sublease, to renew this Sublease, to purchase the Premises, or to lease or purchase adjacent property which Sublessor may own or in which Sublessor has an interest, then Sublessor shall pay to Broker a fee in accordance with the schedule of Broker in effect at the time of the execution of this Sublease. Notwithstanding the foregoing, Sublessor's obligation under this Paragraph 10.2 is limited to a transaction in which Sublessor is acting as a Sublessor, lessor or seller.



10.3 Master Lessor agrees that if Sublessee shall exercise any option or right of first refusal granted to Sublessee by Master Lessor in connection with this Sublease, or any option or right substantially similar thereto, either to extend or renew the Master Lease, to purchase the Premises or any part thereof, or to lease or purchase adjacent property which Master Lessor may own or in which Master Lessor has an interest, or if Broker is the procuring cause of any other lease or sale entered into between Sublessee and Master Lessor pertaining to the Premises, any part thereof, or any adjacent property which Master Lessor owns or in which it has an interest, then as to any of said transactions, Master Lessor shall pay to Broker a fee, in cash, in accordance with the schedule of Broker in effect at the time of the execution of this Sublease.

10.4 Any fee due from Sublessor or Master Lessor hereunder shall be due and payable upon the exercise of any option to extend or renew, upon the execution of any new lease, or in the event of a purchase, at the close of escrow.

10.5 Any transferee of Sublessor's interest in this Sublease, or of Master Lessor's interest in the Master Lease, by accepting an assignment thereof, shall be deemed to have assumed the respective obligations of Sublessor or Master Lessor under this Paragraph 10. Broker shall be deemed to be a third-party beneficiary of this paragraph 10.

11. ATTORNEY'S FEES. If any party or the Broker named herein brings an action to enforce the terms hereof or to declare rights hereunder, the prevailing party in any such action, on trial and appeal, shall be entitled to his reasonable attorney's fees to be paid by the losing party as fixed by the Court.

12. ADDITIONAL PROVISIONS. (If there are not additional provisions, draw a line from this point to the next printed word after the space left here. If there are additional provisions place the same here.) \*Addendum paragraph 13 through 17, Exhibit "A" Parking Plan, and Exhibit 1 (Master Lease)

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ATTENTION: NO REPRESENTATION OR RECOMMENDATION IS MADE BY THE AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION OR BY ANY REAL ESTATE BROKER AS TO THE LEGAL SUFFICIENCY, LEGAL EFFECT, OR TAX CONSEQUENCES OF THIS SUBLEASE OR THE TRANSACTION TO WHICH IT RELATES. THE PARTIES AND URGED TO:

- 1. SEEK ADVICE OF COUNSEL AS TO THE LEGAL AND TAX CONSEQUENCES OF THE SUBLEASE.

RETAIN APPROPRIATE CONSULTANTS TO REVIEW AND INVESTIGATE THE CONDITION OF THE PREMISES. SAID INVESTIGATION SHOULD INCLUDE BUT NOT BE LIMITED TO: THE POSSIBLE PRESENCE OF HAZARDOUS SUBSTANCES, THE ZONING OF THE PROPERTY, THE STRUCTURAL INTEGRITY, THE CONDITION OF THE PROOF AND OPERATING SYSTEMS, AND THE SUITABILITY OF THE PREMISES FOR SUBLESSEE'S INTENDED USE.

WARNING: IF THE SUBJECT PROPERTY AS LOCATED IN A STATE OTHER THAN CALIFORNIA, CERTAIN PROVISIONS OF THE SUBLEASE MAY NEED TO BE REVISED TO COMPLY WITH THE LAWS OF THE STATE IN WHICH THE PROPERTY IS LOCATED.

Executed at: Scottsdale, Arizona SHR Perceptual Management, an Arizona Corporation
on: April 1998 By /s/ CHARLES P. STANFORD, JR.
Address: 8802 E. Doubletree Ranch Rd., By Charles P. Stanford, Jr.
Suite 200 Senior Vice President & C.F.O.
Scottsdale, AZ 85258 (Sublessor) (Corporate Seal)

Executed at: Camarillo, California Pacific Softworks, Inc., a California Corporation
on: April 1998 By /s/ JULIE WHITE
Address: 4000 Via Pescador Julie White, V.P.
Camarillo, CA 93012 By /s/ JOSEPH LECHMAN
Joseph Lechman, Secretary President
"Sublessee" (Corporate Seal)

Executed at: Frank D. McDonald dba Rancho Conejo Properties
on: April 1998 By
Address: By Frank D. McDonald
"Master Lessor" (Corporate Seal)

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 So. Flower St., Suite 500, Los Angeles, CA 90017. (213) 687-8777.

ADDENDUM TO THAT STANDARD SUBLEASE DATED APRIL 7, 1998 FOR THAT CERTAIN PROPERTY COMMONLY KNOWN AS 703 RANCHO CONEJO BLVD., NEWBURY PARK, CALIFORNIA IN WHICH SHR PERCEPTUAL MANAGEMENT, AN ARIZONA CORPORATION IS THE SUBLESSOR AND PACIFIC SOFTWORKS, INC., A CALIFORNIA CORPORATION IS THE SUBLESSEE.

13. IMPROVEMENTS  
BY SUBLESSOR:

Prior to the commencement of the sublease term, the Sublessor shall, at its sole cost and expense, make the following alterations to the premises:

- A. Remove film coating from windows returning perimeter windows to clear glass.
- B. Repaint interior of subject premises. Sublessee to have choice of color.
- C. Remove surface plate in center of warehouse and match VCT tile.
- D. Repaint exterior tilt-up wall other than that which is exposed aggregate.
- E. Clean and polish tile and hardwood floor.
- F. Black background dividers to be left in premises for Sublessee's use.
- G. Replace any damaged or stained ceiling tiles.
- H. Service roof, repairing any leaks.
- I. Replace fluorescent light bulbs where necessary.

Sublessor agrees to provide Sublessee with a work schedule as soon as it receives it.

14. EARLY ACCESS:

Sublessor shall grant Sublessee fifteen (15) days early access to the premises for the purpose of installing telephone and computer lines, furniture, fixtures and equipment. Any such access by Sublessee shall be subject to all of the terms, covenants and conditions of the Sublease other than the payment of rent during the period thereof. Sublessee agrees not to interfere, as the result of such access, with the work of Sublessor or its agents and employees in the completion of the modifications required of Sublessor hereunder. Sublessor shall have no liability to Sublessee for any such equipment or merchandise of Sublessee situated within the premises during the period of such access.

15. RENT ADJUSTMENTS:

The Base Rent shall be increased to the following amounts on the dates set forth below:

May 1, 1999	\$8,825.77 per month
May 1, 2000	\$9,178.80 per month

16. HAZARDOUS  
MATERIALS:

As in any real estate transaction, it is recommended that you consult with a professional such as a civil engineer, industrial hygienist or other person, with experience in evaluating the condition of the property including the possible presence of asbestos, hazardous materials and underground storage tanks. Owner agrees to disclose to Broker and to prospective purchasers and tenants any and all information which Owner has regarding present and future zoning and environmental matters affecting the Property and regarding the condition of

the Property including, but not limited to, structural, mechanical and soils conditions, the presence and location of asbestos, PCB transformers, other toxic, hazardous or contaminated substances, and underground storage tanks, in, on, or about the Property. Broker is authorized to disclose any such information to prospective purchasers or tenants.

17. ADA: Please be advised that an owner or tenant of real property may be subject to the Americans With Disabilities Act (the ADA), a Federal law codified at 42 USC Section 12101 et seq. Among other requirements of the ADA that could apply to your property, Title III of the ADA requires owners and tenants of "public accommodations" to remove barriers to access by disabled persons and provide auxiliary aids and services for hearing, vision or speech impaired persons by January 26, 1992. The regulations under Title III of the ADA are codified at 28 CFR Part 36. We recommend you review the ADA and regulations, as CB Commercial cannot give you legal advice on these issues.

EXHIBIT A  
PARKING PLAN

[SITE PLAN GRAPHIC]

STANDARD INDUSTRIAL/COMMERCIAL SINGLE-TENANT LEASE--NET  
(Do not use this form for Multi-Tenant Property)

1. BASIC PROVISIONS ("BASIC PROVISIONS")

1.1 PARTIES: This Lease ("Lease"), dated for reference purposes only, March 31, 1995, is made by and between Frank D. McDonald, dba Rancho Conejo Properties ("Lessor") and SHR Perceptual Management, an Arizona Corporation ("Lessee"), (collectively the "PARTIES," or individually a "PARTY").

1.2 PREMISES: That certain real property, including all improvements therein or to be provided by Lessor under the terms of this Lease, and commonly known by the street address of 703 Rancho Conejo Boulevard located in the County of Ventura, State of California 91320 and generally described as (describe briefly the nature of the property) a concrete tilt-up industrial building consisting of approximately 11,468 square feet situated on approximately 31,588 square feet of M-1 zoned land. ("PREMISES"), (See Paragraph 2 for further provisions.)

1.3 TERM: five (5) years and four (4) months ("ORIGINAL TERM") commencing May 15, 1995 ("COMMENCEMENT DATE") and ending September 15, 2000 ("EXPIRATION DATE"), (See Paragraph 3 for further provisions.)

1.4 EARLY POSSESSION: May 1, 1995 ("EARLY POSSESSION DATE"). (See Paragraph 3.2 and 3.3 for further provisions.)

1.5 BASE RENT: \$7,224.84 per month ("BASE RENT"), payable on the first day of each month commencing May 1, 1995 (See Paragraph 4 for further provisions.)

/X/ If this box is checked, there are provisions in this LEASE for the BASE RENT to be adjusted.

1.6 BASE RENT PAID UPON EXECUTION: \$7,224.84 as Base Rent for the period May 15-31, 1995 and September 1-15, 2000.

1.7 SECURITY DEPOSIT: \$7,224.84 ("SECURITY DEPOSIT"). (See Paragraph 5 for further provisions.)

1.8 PERMITTED USE: Industrial design and fabrication of prototypes for the automotive industry. (See Paragraph 6 for further provisions.)

1.9 INSURING PARTY: Lessee is the "INSURING PARTY" unless otherwise stated herein. (See Paragraph 8 for further provisions.)

1.10 REAL ESTATE BROKERS: The following real estate brokers (collectively, the "BROKERS") and brokerage relationships exist in this transaction and are consented to by the Parties (check applicable boxes):

CB Commercial Real Estate Group, Inc. represents

/X/ Lessor exclusively ("LESSOR'S BROKER"); / / both Lessor and Lessee, and Capital Commercial Real Estate represents

/X/ Lessee exclusively ("LESSEE'S BROKER"); / / both Lessee and Lessor. (See Paragraph 15 for further provisions.)

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

1.12 ADDENDA. Attached hereto is an Addendum or Addenda consisting of Paragraphs 49 through 53 and Exhibit "A" Parking Area and Exhibit "B" Tenant Improvement Plan all of which constitute a part of this Lease.

2. PREMISES.

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, is an approximation which Lessor and Lessee agree is reasonable and the rental based thereon is not subject to revision whether or not the actual square footage is more or less.

2.2 CONDITION. Lessor shall deliver the Premises to Lessee clean and free of debris on the Commencement Date and warrants to Lessee that the existing plumbing, fire sprinkler system, lighting, air conditioning, heating, and loading doors, if any, in the Premises, other than those constructed by Lessee, shall be in good operating condition on the Commencement Date. If a non-compliance with said warranty exists as of the Commencement Date. Lessor shall, 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 Lessee does not give Lessor written notice of a non-compliance with this warranty within thirty (30) days after the Commencement Date, correction of that non-compliance shall be the obligation of Lessee at Lessee's sole cost and expense.

2.3 COMPLIANCE WITH COVENANTS, RESTRICTIONS AND BUILDING CODE. Lessor warrants to Lessee that the improvements on the Premises comply with all applicable covenants or restrictions of record and applicable building codes, regulations and ordinances 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. If the Premises do not comply with said warranty, Lessor shall, 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 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. See Addendum.

2.4 ACCEPTANCE OF PREMISES. Lessee hereby acknowledges: (a) that it has been advised by the Brokers 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, compliance with Applicable Law as defined in Paragraph 6.3) 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 and assumes all responsibility therefor as the same relate to Lessee's occupancy of the Premises and/or the term 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 the said matters other than as set forth in this Lease.

2.5 LESSEE 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.

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, however, (including but not limited to the obligations to pay Real Property and insurance premiums and to maintain the Premises) shall be in effect during such period. Any such early possession shall not affect nor advance the Expiration Date of the Original Term.

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Exhibit 1

3.3 DELAY IN POSSESSION. If for any reason Lessor cannot deliver possession of the Premises to Lessee as agreed herein by the Early Possession Date. If one is specified in Paragraph 1.4, or, if no Early Possession Date is specified, by the Commencement Date, 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, except as otherwise provided herein, be obligated to pay rent or perform any other obligation of Lessee under the terms of this Lease until Lessor delivers possession of the Premises to Lessee. If possession of the Premises is not delivered to Lessee within sixty (60) days after the Commencement Date, Lessee may, at its 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 if such written notice by Lessee is not received by Lessor within said ten (10) day period, Lessee's right to cancel this Lease shall terminate and be of no further force or effect. Except as may be otherwise provided, and regardless of when the term actually commences, if possession is not tendered to Lessee when required by this Lease and Lessee does not terminate this Lease, as aforesaid, the period free of the obligation to pay Base Rent, if any, that Lessee would otherwise have enjoyed shall run from the date of delivery of possession and continue for a period equal to what Lessee would otherwise have enjoyed under the terms hereof, but minus any days of delay caused by the acts, changes or omissions of Lessee.

#### 4. RENT.

4.1 BASE RENT. Lessee shall cause payment of Base Rent and other rent or charges, as the same may be adjusted from time to time, to be received by 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 (1) full calendar month shall be prorated based upon the actual number of days of the calendar 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.

5. SECURITY DEPOSIT. Lessee shall deposit with Lessor upon 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 therefor deposit moneys 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 moneys with Lessor sufficient to maintain the same ratio between the Security Deposit and the Base Rent as those amounts are specified in the Basic Provisions. 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 moneys to be paid by Lessee under this Lease.

#### 6. USE.

6.1 USE. Lessee shall use and occupy the Premises only for the purposes set forth in Paragraph 1.8, or any other use which is comparable thereto, and for no other purpose. Lessee shall not use or permit the use of the Premises in a manner that creates waste or a nuisance, or that disturbs owners and/or occupants of, or causes damage to, neighboring premises or properties. Lessor hereby agrees to not unreasonably withhold or delay its consent to any written request by Lessee, Lessee's assignees or subtenants, and by prospective assignees and subtenants of the Lessee, its assignees and subtenants, for a modification of said permitted purpose for which the premises may be used or occupied, so long as the same will not impair the structural integrity of the improvements on the Premises, the mechanical or electrical systems therein, is not significantly more burdensome to the Premises and the improvements thereon, and is otherwise permissible pursuant to this Paragraph 6. If Lessor elects to withhold such consent, Lessor shall within five (5) business days give a written notification of same, which notice shall include an explanation of Lessor's reasonable 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, 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 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, by-products or fractions thereof. Lessee shall not engage in any activity in, on 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 Law (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. Reportable Use shall also include Lessee's being responsible for the presence in, on or about the Premises of a Hazardous Substance with respect to which any Applicable Law requires 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 in compliance with all Applicable Law, use any ordinary and customary materials reasonably required to be used by Lessee in the normal course of Lessee's business permitted on the Premises, 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 the use or presence of any Hazardous Substance, activity or storage tank 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 therefrom or therefor, including, but not limited to, the installation (and 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. See Addendum.

(b) DUTY TO INFORM LESSOR. If Lessee knows, or has reasonable cause to believe, that a Hazardous Substance, or a condition involving or resulting from same, 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. Lessee shall also immediately give Lessor 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, or persons entering or occupying the Premises, concerning the presence, spill, release, discharge of, or exposure to, any Hazardous Substance or contamination in, on, or about the Premises, including but not limited to all such documents as may be involved in any Reportable Uses involving the Premises.

(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 loss of rents and/or damages, liabilities, judgments, costs, claims, liens, expenses, penalties, permits and attorney's and consultant's fees arising out of or involving any Hazardous Substance or storage tank brought onto the Premises by or for Lessee or under Lessee's control. Lessee's obligations under this Paragraph 6 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 consultant's and attorney's 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 ??? respect to Hazardous Substances or storage tanks, unless specifically so agreed by Lessor in writing at the time of such agreement.

6.3 LESSEE'S COMPLIANCE WITH LAW. Except as otherwise provided in this Lease, Lessee, shall, at Lessee's sole cost and expense, fully, diligently and in a timely manner, comply with all "APPLICABLE LAW," which term is used in this Lease to include 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 or storage tank), now in effect or which may hereafter come into effect and whether or not reflecting a change in policy from any previously existing policy. 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 Law 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 Law.

6.4 INSPECTION; COMPLIANCE. Lessor and Lessor's Lender(s) (as defined in Paragraph 8.3(a)) 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 Laws (as defined in Paragraph 6.3), and to employ experts and/or consultants in connection therewith and/or to advise Lessor with respect to Lessee's activities, including but not limited to the installation, operation, use, monitoring, maintenance, or removal of any Hazardous Substance or storage tank 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, violation of Applicable Law, or a contamination, caused or materially contributed to by Lessee is found to exist or 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 any 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. See Addendum.

??? MAINTENANCE; REPAIRS; Utility Installations; Trade Fixtures and Alterations.

7.1 LESSEE'S OBLIGATIONS.

(a) Subject to the provisions of Paragraphs 2.2 (Lessor's warranty as to condition), 2.3 (Lessor's warranty as to compliance with covenants, etc),

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 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 and this Lease shall continue in full force and effect, but subject to Lessor's rights under Paragraph 13). 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 giving 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 Lessee's said 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 and 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 a Premises Total Destruction occurs (including any destruction required by any authorized public authority), this Lessee 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 8.6.

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 (1) 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 within twenty (20) days following the occurrence of the damage, or before the expiration of the time provided in such option for its exercise, whichever is earlier ("EXERCISE PERIOD"), (i) exercising such option and (ii) providing Lessor with any shortage in insurance proceeds (or adequate assurance thereof) needed to make the repairs. If Lessee duly exercises such option during said Exercise 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 said Exercise Period, then Lessor may at Lessor's option terminate this Lease as of the expiration of said sixty (60) day period following the occurrence of such damage by giving written notice to Lessee of Lessor's election to do so within ten (10) days after the expiration of the Exercise Period, notwithstanding any term or provision in the grant of option to the contrary.

#### 9.6 ABATEMENT OF RENT; LESSEE'S REMEDIES.

(a) In the event of damage described in Paragraph 9.2 (Partial Damage - Insured), whether or not Lessor or Lessee repairs or restores the Premises, the Base rent, Real Property Taxes, insurance premiums, and other charges, if any, payable by Lessee hereunder for the period during which such damage, its repair or the restoration continues (not to exceed the period for which rental value insurance is required under Paragraph 8.3(b)), shall be abated in proportion to the degree to which Lessee's use of the Premises is impaired. Except for abatement of Base Rent, Real Property Taxes, insurance premiums, 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 repair 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 receipt of such notice, this Lease shall continue in full force and effect. "COMMENCE" as used in this Paragraph 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 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 Law and this Lease shall continue in full force and effect, but subject to Lessor's rights under 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 giving 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 investigation and remediation of such Hazardous Substance Condition totally at Lessee's expense and without reimbursement from Lessor except to the extent of 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 Lessee's said commitment, 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 and the required funds are available. If Lessee does not give such notice and provide the required funds or assurance thereof within the times specified above, this Lease shall terminate as of the date specified in Lessor's notice of termination. If a Hazardous Substance Condition occurs for which Lessee is not legally responsible, there shall be abatement of Lessee's obligations under this Lease to the same extent as provided in Paragraph 9.6(a) for a period of not to exceed twelve (12) months.

9.8 TERMINATION - ADVANCE PAYMENTS. Upon termination of this Lease pursuant to this 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 under the terms of this Lease.

9.9 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 (a) PAYMENT OF TAXES. Lessee shall pay the Real Property Taxes, as defined in Paragraph 10.2, applicable to the Premises during the term of this Lease. Subject to Paragraph 10.1(b), all such payments shall be made at least ten (10) days prior to the delinquency date of the applicable installment. Lessee shall promptly furnish Lessor with satisfactory evidence that such taxes have been paid. If any such taxes to be paid by Lessee shall cover any period of time prior to or after the expiration or earlier termination of the term hereof, Lessee's share of such taxes shall be equitably prorated to cover only the period of time within the tax fiscal year this Lease is in effect, and Lessor shall reimburse Lessee for any overpayment after such proration. If Lessee shall fail to pay any Real Property Taxes required by this Lease to be paid by Lessee, Lessor shall have the right to pay the same, and Lessee shall reimburse Lessor therefor upon demand. See Addendum. (1/2 DEC 10; 1/2 APR 10)

(b) ADVANCE PAYMENT. In order to insure payment when due and before delinquency of any or all Real Property Taxes, Lessor reserves the right, in the event of Lessee's breach of the Lease, to estimate the current Real Property Taxes applicable to the Premises, and to require such current year's Real Property Taxes to 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 that equal monthly amount which, over the number of months remaining before the month in which the applicable tax installment would become delinquent (and without interest thereon), would provide a fund large enough to fully discharge before delinquency the estimated installment of taxes to be paid. When the actual amount of the applicable tax bill is known, the amount of such equal monthly advance payment shall be adjusted as required to provide the funds needed to pay the applicable taxes before delinquency. If the amounts paid to Lessor by Lessee under the provisions of this Paragraph are insufficient to discharge the obligations of Lessee to pay such Real Property Taxes as the same become due. Lessee shall pay to Lessor, upon Lessor's demand, such additional sums as are necessary to pay such obligations. All moneys paid to Lessor under this Paragraph may be intermingled with other moneys of Lessor and shall not bear interest. In the event of a Breach by Lessee in the performance of the obligations of Lessee under this Lease, then any balance of funds paid to Lessor under the provisions of this Paragraph may, subject to proration as provided in Paragraph 10.1(a), at the option of Lessor, be treated as an additional Security deposit under Paragraph 5.

10.2 DEFINITION OF "REAL PROPERTY TAXES." 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 Premises 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 Premises or in the real property of which the Premises are a part, 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 Premises 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.

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 percent assessed, such proportion to be determined by Lessor from the respective valuations

signed 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.

10.4 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 of Lessee contained in the Premises or elsewhere. When possible, Lessee shall cause its 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 personal property shall be assessed with Lessor's real property. Lessee shall pay 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 or, at Lessor's option, as provided in Paragraph 10.1(b).

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 with other premises.

## 12. ASSIGNMENT AND SUBLETTING.

### 12.1 LESSOR'S CONSENT REQUIRED.

(a) Lessee shall not voluntarily or by operation of law assign, transfer, mortgage, mortgage or otherwise transfer or encumber (collectively, "ASSIGNMENT") 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 Lessee 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 the execution by Lessor 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(c), or a noncurable Breach without the necessity of any notice and grace period. If Lessor elects to treat such unconsented to assignment or subletting as a noncurable 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 to fair market rental value or one hundred ten percent (110%) of the Base Rent then in effect, whichever is greater. 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 market value adjustment, (1) 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 (without the Lessee 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, whichever is greater, (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 market rental bears to the Base Rent in effect immediately prior to the market value adjustment.

(e) Lessee's remedy for any breach of this Paragraph 12.1 by Lessor shall be limited to compensatory damages and 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, or (iii) after 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 or 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 sublessee. However, Lessor may consent to subsequent sublettings and assignments of the sublease or any amendments or modifications thereto without notifying Lease 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 sublease.

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

(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 current monthly Base Rent, 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 reasonable 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 12.1(c) shall give Lessor the right (but not the obligation) to require that the Security Deposit be increased to an amount equal to six (6) times the then monthly Base Rent, and Lessor may make the actual receipt by Lessor of the amount required to establish such Security Deposit 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 structure of the rent payable under this Lease be adjusted to what is then the market value and/or adjustment structure for property similar to the Premises as then constituted.

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 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 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 said 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 sublease to atturn 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 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. 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" is defined as a failure by the Lessee to observe, comply with or perform any of the terms, covenants, conditions or rules applicable to Lessee under this Lease. A "BREACH"



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, 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 or any other monetary payment required to be made by Lessee hereunder, whether to Lessor or to a third party, 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 Law 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(b), (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 (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.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 (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 by Lessor that any financial statement given to Lessor by Lessee or any Guarantor of Lessee's obligations hereunder 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 breach basis, and Lessee's failure, within sixty (60) days following written notice by or on behalf of Lessor to Lessee of any such event, to provide Lessor with 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 affirmative duty or obligation of Lessee under this Lease, within (10) days after written notice to Lessee (or in case of 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 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 the leasing commission paid by Lessor 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 prior sentence shall be computed by discounting such amount at the discount rate of the Federal Reserve Bank of San Francisco 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. 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 therein 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 subparagraphs 13.1(b), (c) or (d). In such case, the applicable grace period under subparagraphs 13.1(b), (c) or (d) and 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 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 abandonment and recover the rent as it becomes due, provided Lessee has the right to sublet or assign, subject only to reasonable limitations. See Paragraphs 12 and 36 for the limitations on assignment and subletting which limitations Lessee and Lessor agree 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 the 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.

(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.

**13.3 INDUCEMENT RECAPTURE IN EVENT OF BREACH.** Any agreement by Lessor for free or abated rent or other changes applicable to the Premises, or for the giving or paying by Lessor to or for Lessee of any cash or other bonus, inducement or consideration for Lessee's entering into this Lease, all of which concessions are hereinafter referred to as "INDUCEMENT PROVISIONS," shall be deemed conditioned upon Lessee's full and faithful performance of all of the terms, covenants and conditions of this Lease to be performed or observed by Lessee during the term hereof as the same may be extended. Upon the occurrence of a Default of this Lease by Lessee, as defined in Paragraph 13.1, any such inducement Provision shall automatically be deemed deleted from this Lease and of no further force or effect, and any rent, other charge, bonus, inducement or consideration theretofore abated, given or paid by Lessor under such an inducement Provision shall be immediately due and payable by Lessee to Lessor, and recoverable by Lessor as additional rent due under this Lease, notwithstanding any subsequent cure of said Default by Lessee. The acceptance by Lessor of rent or the cure of the Default which initiated the operation of this Paragraph shall not be deemed a waiver by Lessor of the provisions of this Paragraph unless specifically so stated in writing by Lessor at the time of such acceptance.

**13.4 LATE CHARGES.** Lessee hereby acknowledges that late payment by Lessee to Lessor or 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 trust deed covering the Premises. Accordingly, if any installment of rent or any other sums due from Lessee shall not be received by Lessor or Lessor's designee within five (5) 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 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 the holders of any ground lease, mortgage or deed of trust covering the Premises 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 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

control 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 land area not occupied by any building, is taken by condemnation, and the Premises are not habitable for Lessee's use. 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 fifteen (15) 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 building located on the Premises. No reduction of Base Rent shall occur if the only portion of the Premises taken is land on which there is no building. 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 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 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 the legal and other expenses incurred by Lessor in the condemnation matter, 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 be responsible for the payment of any amount in excess of such net severance damages required to complete such repair.

#### 15. BROKER'S FEE.

15.1 The Brokers named in Paragraph 1.10 are the procuring causes of this Lease.

15.2 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 written agreement between Lessor and said Brokers (or in the event there is no separate written agreement between Lessor and said Brokers, the sum of \$\_\_\_\_\_ as per agreement) for brokerage services rendered by said Brokers to Lessor in this transaction.

15.3 Unless Lessor and Brokers have otherwise agreed in writing, Lessor further agrees that: (a) if Lessee exercises any Option (as defined in Paragraph 39.1) or any Option subsequently granted which is substantially similar to an Option granted to Lessee in this Lease, or (b) if Lessee acquires any rights to the Premises or other premises described in this Lease which are substantially similar to what Lessee would have acquired had an Option herein granted to Lessee been exercised, or (c) if Lessee remains in possession of the Premises, with the consent of Lessor, after the expiration of the term of this Lease after having failed to exercise an Option, or (d) if said Brokers are the procuring cause of any other lease or sale entered into between the Parties pertaining to the Premises and/or any adjacent property in which Lessor has an interest, or (e) if Base Rent is increased, whether by agreement or operation of an escalation clause herein, then as to any of said transactions. Lessor shall pay said Brokers a fee in accordance with the schedule of said Brokers in effect at the time of the execution of this Lease.

15.4 Any buyer or 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 Broker shall be a third party beneficiary of the provisions of this Paragraph 15 to the extent of its interest in any commission arising from this Lease and may enforce that right directly against Lessor and its successors.

15.5 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 named in Paragraph 1.10) in connection with the negotiation of this Lease and/or the consummation of the transaction contemplated hereby, and that no broker or other person, firm or entity other than said named Brokers is entitled to any commission or finder's fee in connection with said transaction. 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, attorneys' fees reasonably incurred with respect thereto.

15.6 Lessor and Lessee hereby consent to and approve all agency relationships, including any dual agencies, indicated in Paragraph 1.10.

#### 16. TENANCY STATEMENT.

16.1 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 "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 If Lessor desires to finance, refinance, or sell the Premises, any part thereof, or the building of which the Premises are a part, Lessee and all Guarantors of Lessee's performance hereunder 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, 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 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, 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 thirty (30) days following the date on which it was due, shall bear interest from the thirty-first (31st) day after it was due at the rate of 12% per annum, but not exceeding the maximum rate allowed by law, in addition to the 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; 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. 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. Brokers have no responsibility with respect thereto or with respect to any default or breach hereof by either Party.

23. NOTICES.

23.1 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, 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 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 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 confirmation or receipt of the transmission thereof, provided a copy is also delivered via delivery or mail. If notice is received on a Sunday or 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 of any other term, covenant or condition hereof. 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 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 preceding Default or Breach by Lessee of any provision hereof, other than the failure of Lessee to pay the particular rent so accepted. Any payment given Lessor by Lessee may be accepted by Lessor on account of moneys 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.

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; ATTORNMEN; 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 and allow such Lender thirty (30) days following receipt of such notice for the cure of said default before invoking any remedies Lessee may have by reason thereof, 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 ATTORNMEN. 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 all 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 the 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 herein.

31. ATTORNEY'S FEES. If any Party or Broker brings an action or proceeding to enforce the terms hereof or declare rights hereunder, the Prevailing Party (as herein defined) or Broker in any such proceeding, action, or appeal thereon, shall be entitled to reasonable attorney's 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 attorney's fees award shall not be computed in accordance with any court fee schedule, but shall be such as to fully reimburse all attorney's fees reasonably incurred. Lessor shall be entitled to attorney's 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.

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, and making such alterations, repairs, improvements or additions to the Premises or to the building of which they are a part, 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 twenty (120) 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 Premises, 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. 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 and the right to install, and all revenues from the installation of, such advertising signs on the Premises, including the roof, as do not unreasonably interfere with the conduct of Lessee's business.

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. Lessors 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 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' or other consultant's 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, practice or storage tank, shall be paid by Lessee to Lessor upon receipt of an invoice and supporting documentation therefor. Subject to Paragraph 12.2(e) (applicable to assignment or subletting), 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. Except as otherwise provided, 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 acknowledgement 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 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.

#### 37. GUARANTOR.

37.1 If there are to be any Guarantors of this Lease per Paragraph 1.11, the form of the guaranty to be executed by each such Guarantor shall be in the form most recently published by the American Industrial Real Estate Association, and each said Guarantor shall have the same obligations as Lessee under this Lease, including but not limited to the obligation to provide the Tenancy Statement and information called for by Paragraph 16.

37.2 It shall constitute a Default of the Lessee under this Lease if any such Guarantor fails or refuses, upon reasonable request by Lessor to give: (a) evidence of the due execution of the guaranty called for by this Lease, including the authority of the Guarantor (and of the party signing on Guarantor's behalf) to obligate such Guarantor on said guaranty, together with a certificate of incumbency showing the signature of the persons authorized to sign on its behalf, (b) current financial statements of Guarantor as may from time to time be requested by Lessor, (c) a Tenancy Statement, or (d) written confirmation that the guaranty is still in effect.

38. QUIET POSSESSION. Upon payment by Lessee of the rent for the Premises and the observance 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 of the Premises for the entire term hereof subject to all of the provisions of this Lease.

#### 39. OPTIONS.

39.1 DEFINITION. AS used in this Paragraph 39 the word "Option" has the following meaning: (a) the right 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; (b) the 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 property of Lessor or the right of first offer to lease other property Lessor; (c) the right to purchase the Premises, or the right of first refusal to purchase the Premises, or the right of first offer to purchase the Premises, or the right 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 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 Default under Paragraph 13.1. whether or not the Defaults are cured, during the twelve (12) 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) 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 Default 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. MULTIPLE BUILDINGS. If the Premises are part of a group of buildings controlled by Lessor, Lessee agrees that it will abide by, keep and observe all reasonable 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 such other buildings and their invitees, 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. 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 Lessor or Lessor's agent and submission of same to Lessee shall not be deemed an offer to lease to Lessee. This Lease is not intended to be binding until executed 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.

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.

IF THIS LEASE HAS BEEN FILLED IN, IT HAS BEEN PREPARED FOR SUBMISSION TO YOUR ATTORNEY FOR HIS APPROVAL. FURTHER, EXPERTS SHOULD BE CONSULTED TO EVALUATE THE CONDITION OF THE PROPERTY AS TO THE POSSIBLE PRESENCE OF ASBESTOS, STORAGE TANKS OR HAZARDOUS SUBSTANCES. NO REPRESENTATION OR RECOMMENDATION IS MADE BY THE AMERICAN INDUSTRIAL REAL ESTATE ASSOCIATION OR BY THE REAL ESTATE BROKER(S) OR THEIR 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 LOCATED 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 on the dates specified above to their respective signatures.

Executed at Durango, Colorado

on May , 1995

by LESSOR: Frank D. McDonald

By /s/ FRANK D. McDONALD

Name Printed:

Title:

By

Name Printed:

Title:

Address:

Tel. No. ( ) Fax No. ( )

Executed at Scottsdale, Arizona

on May , 1995

by LESSEE: SHR Perceptual Management, an Arizona Corporation

By /s/ BARRY SHEPARD

Name Printed: Barry Shepard

Title: President

By

Name Printed:

Title:

Address:

Tel. No. ( ) Fax No. ( )

NOTICE: These forms are often modified to meet changing requirements of law and industry needs. Always write or call to make sure you are utilizing the most current form: American Industrial Real Estate Association, 345 South Figueroa Street, Suite M-1, Los Angeles, CA 90071. (213) 687-8777. Fax. No. (213) 687-8616

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ADDENDUM TO THAT CERTAIN STANDARD INDUSTRIAL/COMMERCIAL LEASE DATED APRIL 14, 1995, BETWEEN SHR PERCEPTUAL MANAGEMENT, AN ARIZONA CORPORATION, AS LESSEE AND FRANK D. MCDONALD dba RANCHO CONEJO PROPERTIES AS LESSOR FOR THE PREMISES LOCATED AT 703 RANCHO CONEJO BOULEVARD, NEWBURY PARK, CALIFORNIA.

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- 2.3 COMPLIANCE WITH COVENANTS, RESTRICTIONS AND BUILDING CODE -- CONTINUED:  
Lessee shall not be responsible to modify the Premises to comply with such American with Disabilities act ("ADA") unless the specific use of the Lessee requires said compliance.
- 6.2 HAZARDOUS SUBSTANCES -- CONTINUED: Lessee shall not be liable to or required by Lessor to remedy any toxic or hazardous condition which existed on the Premises prior to Lessees occupying the Premises.
- If a Hazardous Substance condition occurs during or after the Term of the lease, Lessee shall not be responsible for remediation unless caused by its officers, employees, agents, contractors, subcontractors, affiliates, lessees, assignees, invitees, or licensees.
- 6.4 INSPECTION: COMPLIANCE -- CONTINUED:  
Notwithstanding this paragraph, Lessor may require Lessee to provide a Phase I Environmental Report on the Premises, at Lessee's sole cost and expense thirty (30) days prior to the expiration of the Lease. Said Environmental Report shall be provided by a licensed Environmental Company acceptable by Lessor.
- 10.1(a) PAYMENT OF TAXES -- CONTINUED:  
Notwithstanding anything contained in this paragraph, Lessee shall have the right to contest the payment of Real Property Taxes with the Ventura County Tax Assessor, provided such taxes are paid in accordance as stated in this lease and Lessor is indemnified from any costs or expenses related to such contest or litigation by Lessee.
49. RENT ADJUSTMENTS:  
See separate addendum attached.
50. OPTION TO EXTEND:  
See separate addendum attached.
51. LANDSCAPED AREAS:  
(a) The term "Landscaped Areas" means all areas within the exterior boundaries of the Premises or adjacent thereto, including the areas within the Premises that are provided and designated by Lessor from time to time to be landscaped. The term landscape shall include without limitation preparation of the soil, hydroseeding, planting of grass sod, shrubs, trees, plants, etc. and the installation of irrigation sprinkler systems, control devices, etc.  
(b) The initial cost of landscaping the Landscaped Areas shall be borne by the Lessor.  
(c) The maintenance of all landscaping in the Landscaped Areas shall be subject to the exclusive control and management of Lessor, or such other persons or nominees as Lessor may designate or assign to exercise such management or control. Lessor shall have the right to:  
(i) Establish and enforce reasonable rules and regulations applicable to all tenants adjacent to the Premises concerning the Landscaped Areas and the maintenance, management and use of the Landscaped Areas.  
(ii) Close temporarily any of the landscaped areas for maintenance purposes.  
(iii) From time to time enter into contract(s) with a landscape maintenance firm or person(s) on such terms and conditions and for such period of time as Lessor deems reasonable and proper both as to service and as to cost.  
(d) Lessor and all persons designated by it will have full and unimpaired access at all times to the Premises for all purposes relating to landscaping or maintaining the landscaping thereon.
52. LESSEE'S SHARE OF LANDSCAPE MAINTENANCE COSTS:  
Lessee shall pay to Lessor as additional rent an amount estimated by Lessor to be Lessee's share of Landscape Maintenance Costs (as defined in this paragraph), on the first day of each month, commencing on the date the term commences, or on the first day of the month following the month the term commences if the term commences on a day other than the first day of a month, as the case may be, and continuing during the

ADDENDUM TO THAT CERTAIN STANDARD INDUSTRIAL/COMMERCIAL LEASE DATED APRIL 14, 1995, BETWEEN SHR PERCEPTUAL MANAGEMENT, AN ARIZONA CORPORATION, AS LESSEE AND FRANK D. MCDONALD dba RANCHO CONEJO PROPERTIES AS LESSOR FOR THE PREMISES LOCATED AT 703 RANCHO CONEJO BOULEVARD, NEWBURY PARK, CALIFORNIA.

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term. Lessee's proportionate share of Landscape Maintenance Costs shall be determined by dividing the total number of square feet of the building on the Premises by the sum of leasable square feet in all building located at 667,703 and 711 Rancho Conejo Boulevard, Newbury Park multiplied by the total monthly Landscape Maintenance Costs. The term "Leasable Square Feet" as used herein shall be deemed to mean the ground floor of all of the three (3) buildings with measurements from outside of exterior walls to center line of demising partitions and including all areas under entrance soffits. For the purpose of this clause, the building on the Premises is deemed to comprise an area of 11,468 square feet. Landscape Maintenance costs that cover a period not within the term of this Lease shall be pro-rated. Lessor can adjust the monthly Landscape Maintenance charge at the end of each accounting period on the basis of Lessor's reasonably anticipated costs for the following accounting period. An accounting period is a period commencing January 1st and ending on December 31st, except that the first accounting period shall commence on the date the term commences and the last accounting period shall end on the date the term expires or terminates. Lessor shall furnish to Lessee a statement showing the total Landscape Maintenance Costs for the accounting period, and the payment made by Lessee with respect to each accounting period, within sixty (60) days after the end of each accounting period. Each statement shall be prepared, signed and certified to be correct by Lessor. If Lessee's share of Landscape Maintenance Costs for the accounting period exceeds the payments made by Lessee, Lessee shall pay to Lessor the deficiency within ten (10) days after receipt of the statement. If Lessee's payments made during the accounting period exceed Lessee's share of Landscape Maintenance Costs, Lessor shall pay Lessee the excess at the time Lessor furnishes the statement to Lessee.

Landscape Maintenance Costs means all sums expended by Lessor for maintenance of the landscaping in the Landscaped Areas and the sweeping of the paved areas and an allowance to Lessor for supervision and administration of and relating to the maintenance of the landscaping in the Landscaped Areas and the sweeping of the parking areas in an amount equal to ten (10%) percent of the total Landscaped Maintenance Costs. Costs for maintenance of landscaping in Landscaped Areas shall include, without limitation, costs of maintenance firms, contractors and persons from maintaining landscaping in Landscaped Areas, of cleaning, sweeping and other janitorial services of the Landscaped Areas and Paved Areas, fertilizing, gardening, planting and re-landscaping, repairing and/or replacing irrigation sprinkler systems, including valves, sprinkler heads, pipes, control devices, all costs of utilities used in connection with the landscaping of Landscaped Areas, reasonable depreciation on machinery and equipment used in connection with landscaping of Landscaped Areas, premiums on public liability and property damage insurance and all other costs necessary in Lessor's judgment for the maintenance of landscaping in Landscaped Areas.

Lessee's percentage of landscape maintenance costs and driveways and parking areas are 31.6%.

53. FREE RENT:

Lessee shall be relieved of its obligation to pay Base Rent for the months of June 1995, July 1995, August 1995 and September 1995.

ADDENDUM TO THAT CERTAIN STANDARD INDUSTRIAL/COMMERCIAL LEASE DATED APRIL 14, 1995, BETWEEN SHR PERCEPTUAL MANAGEMENT, AN ARIZONA CORPORATION, AS LESSEE AND FRANK D. MCDONALD dba RANCHO CONEJO PROPERTIES AS LESSOR FOR THE PREMISES LOCATED AT 703 RANCHO CONEJO BOULEVARD, NEWBURY PARK, CALIFORNIA.

AMERICAN WITH DISABILITIES ACT ("ADA"). "The parties hereto agree to comply with all applicable federal, state and local laws, regulations, codes, ordinances and administrative orders having jurisdiction over the parties, property of the subject matter of this agreement, including, but not limited to the 1964 Civil Rights Act and all amendments thereto, the Foreign Investment In Real Property Tax Act, the Comprehensive Environmental Response Compensation and Liability Act and The Americans With Disabilities Act."

CONSULT YOUR ATTORNEY/ADVISORS - This document has been prepared for approval by your attorney. No representation or recommendation is made by CB Commercial Real Estate Group, Inc. or the Southern California Chapter of the Society of Industrial and Office Realtors (S.I.O.R.), Inc., or the agents or employees of either of them as to the legal sufficiency, legal effect, or tax consequences of this document or the transaction to which it relates. These are questions for your attorney.

In any real estate transaction, it is recommended that you consult with a professional, such as a civil engineer, industrial hygienist or other person, with experience in evaluating the condition of the property, including the possible presence of asbestos, hazardous materials and underground storage tanks.

/s/ FRANK D. MCDONALD  
-----  
LESSOR'S SIGNATURE

5/23/95  
-----  
DATE

/s/ BARRY SHEPARD  
-----  
LESSEE'S SIGNATURE

5/17/95  
-----  
DATE

EXHIBIT A

PARKING PLAN

EXHIBIT B

TENANT IMPROVEMENT PLAN



[LOGO]  
 OPTION(S) TO EXTEND  
 ADDENDUM TO  
 STANDARD LEASE

DATED April 14, 1995  
 -----

BY AND BETWEEN (LESSOR) Frank D. McDonald, dba Rancho Conejo Properties  
 -----  
 (LESSEE) SHR Perceptual Management, an Arizona Corporation  
 -----

PROPERTY ADDRESS: 703 Rancho Conejo Blvd., Newbury Park, CA  
 -----

Paragraph 50

A. OPTION(S) TO EXTEND:

Lessor hereby grants to Lessee the option to extend the term of this Lease for 1 additional 60 month period(s) commencing when the prior term expires upon each and all of the following terms and conditions:

(i) Lessee gives to Lessor, and Lessor actually receives on a date which is prior to the date that the option period would commence (if exercised) by at least 6 and not more than 9 months, a written notice of the exercise of the option(s) to extend this Lease for said additional term(s), time being of essence. If said notification of the exercise of said option(s) is (are) not so given and received, the option(s) shall automatically expire; said option(s) may (if more than one) only be exercised consecutively;

(ii) The provisions of paragraph 39, including the provision relating to default of Lessee set forth in paragraph 39.4 of this Lease are conditions of this Option;

(iii) All of the terms and conditions of this Lease except where specifically modified by this option shall apply;

(iv) 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)

1. COST OF LIVING ADJUSTMENT(S) (COL)

(a) On (Fill in COL Adjustment Date(s): May 1, 2000, May 1, 2001, May 1, 2002, May 1, 2003, May 1, 2004, and May 1, 2005 the monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease 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 -- Anaheim -- Riverside. All items (1982-1984 = 100), herein referred to as "C.P.I."

(b) The monthly rent payable in accordance with paragraph A1(a) 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 C.P.I. of the calendar month 2 (two) months prior to the month(s) specified in paragraph A1(a) above during which the adjustment is to take effect, and the denominator of which shall be the C.P.I. of the calendar month which is two (2) 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 date for rent adjustment and shall increase a minimum of three (3%) percent and a maximum of seven (7%) percent per annum.

(c) In the event the compilation and/or publication of the C.P.I. 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 C.P.I. shall be used to make such calculation. In the event that Lessor and Lessee 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 Arbitrators shall be paid equally by Lessor and Lessee.

OPTION(S) TO EXTEND  
 PAGE 1 OF 2

NOTICE: These forms are often modified to meet changing requirements of law and industry needs. Always write or call to make sure you are utilizing the most current form. American Industrial Real Estate Association, 345 South Figueroa Street, Suite M-1, Los Angeles, CA 90071, (213) 687-8777, Fax No. (213) 687-8616.

C. BROKER'S FEE

The Real Estate Brokers specified in paragraph 1.10 of the attached Lease shall be paid a Brokerage Fee for each adjustment specified above in accordance with paragraph 15 of the attached Lease.

OPTION(S) TO EXTEND  
Page 2 of 2

NOTICE: These forms are often modified to meet changing requirements of law and industry needs. Always write or call to make sure you are utilizing the most current form. American Industrial Real Estate Association, 345 South Figueroa Street, Suite M-1, Los Angeles, CA 90071, (213) 687-8777, Fax No. (213) 687-8616.

[LOGO]

RENT ADJUSTMENT(S)

ADDENDUM TO  
STANDARD LEASE

Dated April 14, 1995  
-----

By and Between (Lessor) Frank D. McDonald, dba Rancho Conejo Properties  
-----

(Lessee) SHR Perceptual Management, an Arizona Corporation  
-----

Property Address: 703 Rancho Conejo Boulevard, Newbury Park, CA  
-----

Paragraph 49  
-----

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 Methods) to be Used and Fill in Appropriately)

I. COST OF LIVING ADJUSTMENT(S) (COL)

(a) On (Fill in COL Adjustment Date(s): May 1, 1996, May 1, 1997, May 1, 1998, May 1, 1999, May 1, 2000, the monthly rent payable under paragraph 1.5 ("Base Rent") of the attached Lease 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):  CPIW (Urban Wage Earners and Clerical Workers) or  CPIU (All Urban Consumers), for (Fill in Urban Area): Los Angeles - Anaheim - Riverside. All items (1982-1984 = 100), herein referred to as "C.P.I."

(b) The monthly rent payable in accordance with paragraph A1(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 C.P.I. of the calendar month 2 (two) months period to the month(s) specified in paragraph A1(a) above during which the adjustment is to take effect, and the denominator of which shall be the C.P.I. of the calendar month which is two (2) 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 of 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 date for rent adjustment and shall increase a minimum of four (4%) percent and maximum of seven (7%) percent per annum.

(c) In the event the compilation and/or publication of the C.P.I. 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 C.P.I. shall be used to make such calculation. In the event that Lessor and Lessee 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 Arbitrators shall be paid equally by Lessor and Lessee.

RENT ADJUSTMENT(S)

NOTICE: These forms are often modified to meet changing requirements of law and industry needs. Always write or call to make sure you are utilizing the most current form. American Industrial Real Estate Association, 345 South Figueroa Street, Suite M-1, Los Angeles, CA 90071, (213) 687-8777, Fax No. (213) 687-8616.

## C. BROKER'S FEE:

The Real Estate Brokers specified in paragraph 1.10 of the attached Lease shall be paid a Brokerage Fee for each adjustment specified above in accordance with paragraph 15 of the attached Lease.

RENT ADJUSTMENT(S)

Page 2 of 2

NOTICE: These forms are often modified to meet changing requirements of law and industry needs. Always write or call to make sure you are utilizing the most current form. American Industrial Real Estate Association, 345 South Figueroa Street, Suite M-1, Los Angeles, CA 90071, (213) 687-8777, Fax No. (213) 687-8616.

## CONSULTING AGREEMENT

THIS CONSULTING AGREEMENT (this "Agreement") is executed as of the 8th day of March, 1996, by and between PACIFIC SOFTWORKS, INC., a California corporation (the "Company") and KENNETH WOODGRIFT ("Consultant") and is made with respect to the following facts:

- A. Consultant is knowledgeable regarding the business of the Company.
- B. The Company desires to obtain the consulting services of Consultant relating to the location of inventory sources, pricing strategies of the Company's products and advertising and promotion strategies using Consultant's extensive expertise and experience with similar products (the "Consulting Services"), and Consultant desires to provide these services to the Company.
- C. Consultant and the Company believe it is in their mutual best interests to enter into this Agreement pursuant to the terms hereinafter set forth.

NOW, THEREFORE, in consideration of the premises and the mutual covenants herein contained, THE PARTIES HERETO AGREE AS FOLLOWS:

1. Term of Agreement. The term of this agreement shall commence as of March 8, 1996 and shall remain in full force and effect, unless terminated as provided in Section 7 of this Agreement, until August 31, 1999.
2. Services of Consultant. The Company hereby engages Consultant and Consultant hereby agrees to perform the Consulting Services as described in Section 3 of this Agreement.
3. Time and Efforts. Consultant agrees that she shall be available to the Company for up to a maximum of fifteen (15) hours per month during the term of this Agreement. The Consulting Services may be performed at any location within or outside Ventura County, California, as Consultant in his sole discretion shall determine. The exact date and time of the Consulting Services shall be as requested by the Company, but subject to the availability of Consultant as determined by Consultant within his sole discretion. If the Company does not request the performance of fifteen (15) hours of Consulting Services for any month during the term of this Agreement, the unused time shall lapse and not be carried forward to the next month.

4. Compensation. During the term of this Agreement, the Company shall pay, in full payment for the Consulting Services hereunder, Six Hundred Thousand Dollars (\$600,000), payable in forty-two [42] equal installments on the first day of each month, commencing March 8, 1996. Consultant shall be entitled to the entire consideration provided hereunder, notwithstanding any early termination of this Agreement. Consultant may, if the Company fails to make any payment when due within five (5) days of when notice of defaults is given to the Company, accelerate payment of all sums due hereunder if the Company fails to pay any installment when due.

5. Expenses. Consultant shall not be obligated to perform any services which would require the incurrence of any expense unless the Company agrees in writing to reimburse the Company for such expenses.

6. Interest. Any sum accruing to Consultant under this Agreement which is not paid when due shall bear interest at the rate of ten percent (10%) per annum from the date due until paid.

7. Termination. This Agreement may only be terminated by the mutual written agreement of Consultant and the Company to terminate. This Agreement shall not be terminated by the death or disability of any employee, officer, director or shareholder of Consultant or by the occurrence of any other event.

8. Independent Contractor. The relationship of Consultant to the Company hereunder shall be that of an independent contractor. The Company shall pay Consultant directly, without payroll deductions of any kind whatsoever. Consultant shall have the responsibility to discharge all of the obligations of an independent contractor under federal, state and local law, including those obligations relating to taxes, unemployment compensation and insurance, Social Security, worker's compensation, disability, pensions and tax withholdings. Nothing contained herein shall be construed to create the relationship between the Company and Consultant of employer and employee.

9. Notices. Unless applicable law requires a different method of giving notice, any and all notices, demands or other communications required or desired to be given hereunder by any party shall be in writing and shall be validly given or made to another party if served personally or if deposited in the United States mail, certified or registered, postage prepaid or if transmitted by telegraph, teletype or other electronic written transmission device. If such notice, demand or other communication is served personally, service shall be conclusively deemed made at the time of such personal service. If such notice, demand or other communication is given by mail, such shall be

conclusively deemed given seventy-two (72) hours after the deposit thereof in the United States mail, or if by telegraph or if by other carrier service, upon confirmation of delivery by the carrier, addressed to the party to whom such notice, demand or other communication is to be given as follows:

To Company: Pacific Softworks, Inc.  
400 Via Pescador  
Camarillo, California 93012

To Consultant: Kenneth Woodgrift  
4205 Romany Drive  
Oxnard, California 93035

With a copy to: Jeffer, Mangels, Butler &  
Marmaro LLP  
2121 Avenue of the Stars  
10th Floor  
Los Angeles, California 90067  
ATTN: Robert E. Braun, Esq.

Any party hereto may change its address for the purpose of receiving notices, demands and other communications as herein provided by a written notice given in the manner aforesaid to the other party or parties hereto.

10. Indemnification. Company hereby agrees to indemnify, defend and hold Consultant harmless from and against any and all claims, actions, demands, lawsuits, causes of action, expenses (including attorneys' fees and court costs), liabilities, interest, taxes, penalties and any and all other damages (collectively, the "Claims") which Consultant may suffer and which result from or arise out of, or are in connection with, any of the acts of Company.

11. Attorneys' Fees. Should any party hereto engage an attorney or institute any action or proceeding at law or in equity, or in connection with an arbitration, to enforce any provision of this Agreement, including an action for declaratory relief, or for damages by reason of an alleged breach of any provision of this Agreement, or otherwise in connection with this Agreement, or any provision thereof, the prevailing party shall be entitled to recover from the losing party or parties actual attorneys' fees and costs for services rendered to the prevailing party in such action or proceeding.

12. Arbitration. Any controversy or claim arising out of, or relating to, this Agreement, or the making, performance or interpretation thereof, shall be settled by arbitration in Ventura County, California in accordance with the rules of the American Arbitration Association then existing, and judgment on

the arbitration award may be entered in any court having jurisdiction over the subject matter of the controversy. The parties further agree that a restraining order, injunction, writ of possession and/or writ of attachment may be applied for from a court of competent jurisdiction by any party pending resolution of the dispute. The arbitrators selected shall be persons experienced in negotiating, making and consummating agreements of the type of this Agreement.

13. Full Authority. Each of the parties and signatories to this Agreement represents and warrants that he or she has the full right, power, legal capacity and authority to enter into and perform the parties' respective obligations hereunder and that such obligations shall be binding upon such party without the requirement of the approval or consent of any other person or entity in connection herewith. Each person signing this Agreement on behalf of an entity represents and warrants that he or she has the full right, power, legal capacity and authority to sign this Agreement on behalf of such entity.

14. Time of the Essence. Time is of the essence of this Agreement, and in all the terms, provisions, covenants and conditions hereof.

15. Applicable Law. This Agreement shall, in all respects, be governed by the laws of the State of California applicable to agreements executed and to be wholly performed within California.

16. Severability. Nothing contained herein shall be construed so as to require the commission of any act contrary to law, and wherever there is any conflict between any provisions contained herein and any present or future statute, law, ordinance or regulation, the latter shall prevail; but the provision of this Agreement which is affected shall be curtailed and limited only to the extent necessary to bring it within the requirements of the law.

17. Further Assurances. Each of the parties hereto shall execute and deliver any and all additional papers, documents and other assurances, and shall do any and all acts and things reasonably necessary in connection with the performance of their obligations hereunder to carry out the intent of the parties hereto.

18. Modifications or Amendments. No amendment, change or modification of this Agreement shall be valid, unless in writing and signed by all of the parties hereto.

19. Successors and Assigns. All of the terms and provisions contained herein shall inure to the benefit of and



shall be binding upon the parties hereto and their respective heirs, legal representatives, successors and assigns.

20. Entire Agreement. This Agreement constitutes the entire understanding and agreement of the parties with respect to its subject matter and any and all prior agreements, understandings or representations with respect to its subject matter are hereby terminated and cancelled in their entirety and are of no further force or effect.

21. Non-Waiver. No waiver by any party hereto of a breach of any provision of this Agreement shall constitute a waiver of any preceding or succeeding breach of the same or any other provision hereof.

22. Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

23. Number and Gender. In this Agreement, the masculine, feminine or neuter gender, and the singular or plural number, shall each be deemed to include the others whenever the context so requires.

24. Captions. The captions appearing at the commencement of the sections hereof are descriptive only and for convenience in reference. Should there be any conflict between any such caption and the section at the head of which it appears, the section and not such caption shall control and govern in the construction of this Agreement.

25. Expenses. Each of the parties shall pay all of their own costs, legal fees, accounting fees, and any other expenses incurred or to be incurred by it or them in negotiating and preparing this Agreement, and closing and carrying out the transactions contemplated by this Agreement.

26. Parties in Interest. Nothing in this Agreement, whether express or implied, is intended to confer any rights or remedies under or by reason of this Agreement on any persons other than the parties and their respective successors and assigns, nor is anything in this Agreement intended to relieve or discharge the obligation or liability of any third persons to any party to this Agreement, nor shall any provision give any third person any right of subrogation or action over or against any party to this Agreement.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written.

"COMPANY"

Pacific Softworks, Inc.  
a California corporation

/s/ GLENN RUSSELL

-----  
Glenn Russell, Secretary

"CONSULTANT"

-----  
Kenneth Woodgrift

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written.

"COMPANY"

Pacific Softworks, Inc.  
a California corporation

-----  
Glenn Russell,  
Secretary

"CONSULTANT"

/s/ KENNETH WOODGRIFT  
-----  
Kenneth Woodgrift

PACIFIC SOFTWARES INC.  
703 Rancho Conejo Blvd  
Newbury Park, CA 91320

January 27, 1999

Mr. Glenn Golenberg  
Golenberg & Co.  
11100 Santa Monica Boulevard  
Suite 990  
Los Angeles, Ca. 90025

Dear Glenn,

This letter is to document the terms of the services performed and to be performed on a nonexclusive basis by Golenberg & Co. for the benefit of Pacific Softwareworks. Pursuant to a letter between Pacific Softwareworks Inc., (the "Company") on the one hand, and Golenberg & Co. and Marc Guren (collectively "Golenberg"), on the other hand dated June 18, 1998 (the "Letter"). Golenberg has previously provided certain services to Pacific Softwareworks. Pacific Softwareworks has paid Golenberg \$30,000. These payments are hereby accepted by Golenberg as payment in full for the cash obligations due under the Letter. In addition, the Letter between the parties provides that Golenberg would receive options on 10% of Pacific Softwareworks' stock with a strike price based on a \$4,000,000 Company value as of June 18, 1998.

This agreement is to clarify and supersede the prior Letter as provided herein as it relates to the options. If, at any time prior to June 18, 1999, Golenberg procures and presents to Pacific Softwareworks a purchaser or financing offer(s) for Pacific Softwareworks, subject to costs, terms, and conditions reasonable and customary in such a proposal, which offer is acceptable by Pacific Softwareworks, then Pacific Softwareworks will thereupon issue to Golenberg as compensation for such services a five year option to purchase shares of Company stock in Pacific Softwareworks that represents 10% of the outstanding shares of the Company as of June 18, 1998, with a strike price based on a total Company value of \$4,000,000. Except for the \$30,000 previously paid by Pacific Softwareworks to Golenberg, or as to out-of-pocket expenses incurred by Golenberg and approved by Pacific Softwareworks, each party will pay their own costs incurred in connection with any purchaser or financing transactions, and neither party shall be responsible for the other party's costs.

Except as otherwise mutually agreed upon in the future, if Golenberg does not produce a purchaser or financing offer as set forth above, then Golenberg shall be entitled to retain as sole compensation the \$30,000 previously paid by Pacific Softwareworks to Golenberg and nothing more.

This agreement supersedes any and all previous understanding and/or agreements, whether written or verbal, and shall not be modified or changed except in writing executed by both parties. It shall bind, obligate and inure to the benefit of the legal successors, transferees, grantees and heirs of each party hereto. Except as set forth in this agreement, both parties agree to release the other from any obligation from previous transactions, understandings, or agreements (including but not

limited to the Letter) and from any and all other claims or liabilities, whether known or unknown, against the other (including against Marc D. Guren).

The parties further agree that any disputes under or relating to this agreement, or performance or nonperformance hereunder, shall exclusively be subject to arbitration pursuant to the Commercial Arbitration Rules of the American Arbitration Association, that the arbitrator shall grant to the prevailing party any and all attorneys' fees and costs and expenses, as well as interest, and that the award shall be enforceable in the courts.

Each party agrees that in any dispute regarding the interpretation or construction of this agreement, no presumption shall operate in favor of or against any party by virtue of its or his role in drafting or not drafting the terms and conditions set forth herein.

Sincerely,

/s/ GLENN RUSSELL                                    03/02/99  
-----

Glenn Russell

Accepted on 3-2-99 by:

/s/ GLENN GOLENBERG  
-----

Golenberg & Co.

[GOLENBERG & CO. LETTERHEAD]

VIA TELEFAX: (805) 484-3929

June 18, 1998

Mr. Glenn Russell  
Pacific Softworks  
703 Rancho Conejo Boulevard  
Neubury Park, California 91320

Dear Glenn,

Just a note to thank you for the time you spent with Marc Guren and me last week. We enjoyed our visit very much, and believe that there are some distinct opportunities for Pacific Softworks. In that regard, we believe that the company must undertake a thorough examination of its current business, as well as strategic direction in the future. This will encompass creating a well thought out business plan and model. Once the model is complete, we will need to examine and evaluate the various options available to achieve these plans. This will include developing a comprehensive financing plan, or exit strategy, which is in the best interest of the current Pacific Softworks shareholders. On our visit, we spent a good amount of time describing to you the actual process, and assuring you that it will take considerable amounts of time and focus.

Because we wish to align ourselves with your interest, we have structured our fee arrangement consistent with creating value on your behalf. In that regard, we would require an option on 10 percent of the currently outstanding, fully diluted shares. This includes all options and warrants outstanding. This option would have an exercise price which would value the company at \$4,000,000. For example, if the company had one million shares outstanding, and had a value of \$4.00 per share, we would get options granted to us for 100,000 shares at \$4.00 per share. This requires our assignment to create values far in excess of \$4,000,000, to make our efforts at all worthwhile.

In addition, for our time spent, and to help defray our overhead costs, we would require a \$10,000 per month retainer for a three-month period. Once the business plan and evaluation are complete, and we have agreed upon a financing plan, we would be involved as your Financial Advisor, in whatever capacity was deemed appropriate. This would largely depend on the nature of the transaction as to whether the company needed to raise money, or was looking to a joint venture partner. These activities might include additional fees, but would be agreed upon at the time such activities took place.

It's important for you to understand that, at all times, you will be in control of the process. We will have input and suggestions, but are keenly aware that this is your company.

We look forward to a long and profitable relationship, and feel quite confident that, after we know all the facts, we can create significant value.

Very truly yours,

/s/ GLENN GOLENBERG

- -----  
Glenn Golenberg

GG:gc

cc: Marc Guren

Our assignment will include reimbursement of all out-of-pocket expenses to be reasonably approved by you. We will begin the cash portion of our arrangement July 1, 1998 and the option portion will begin effective as the date of the signing.

/s/ GLENN RUSSELL 06-22-98

- -----  
Glenn Russell

Approved

## INDEPENDENT AUDITORS' CONSENT

We hereby consent to the use in this Registration Statement of Pacific Softworks, Inc. on Form SB-2 of our report dated January 29, 1999, appearing in the Prospectus, which is a part of such Registration Statement relating to the consolidated financial statements of Pacific Softworks, Inc. and Subsidiary, and to the reference to our Firm under the caption "Experts" in such Prospectus.

/s/ MERDINGER, FRUCHTER, ROSEN & CORSO, P.C.

MERDINGER, FRUCHTER, ROSEN & CORSO, P.C.  
Certified Public Accountants

Los Angeles, California  
May 12, 1999